Week Ahead Economic Preview

Global overview

- **Flash PMIs for the US, Eurozone, UK, Japan and Australia**
- **COVID-19 policy response, including Bank of England Policy meeting**

With the global economy facing recession and markets showing increased signs of stress, flash PMI surveys will be eagerly watched for the extent of the economic impact of the COVID-19 outbreak in March. The March flash PMI data for the US, Eurozone, UK, Japan and Australia follow worldwide PMI surveys which showed the global economy contracting at the steepest rate since 2009 in February as the coronavirus disrupted manufacturing supply chains and hit service sectors such as travel, tourism, restaurants and transport.

In the US, the IHS Markit PMIs will come on the heels of February numbers which had indicated one of the toughest months for business since the global financial crisis. Although recent weeks have seen news of stimulus from both the Federal Reserve and the government, including a slashing of rates to near zero, markets are fearing even worse numbers to come with recession now forecast. Regional Fed surveys and the University of Michigan consumer survey will also be eagerly assessed for virus impact in March (page 3).

The Eurozone and UK PMIs had meanwhile shown surprising resilience in February, but the spread of COVID-19 has since widened markedly into Europe, meaning March flash surveys will likely reflect widespread disruptions to business across the region. The UK flash PMI comes out ahead of the Bank of England's first scheduled Monetary Policy Committee meeting with new governor Andrew Bailey at the helm, although two emergency meetings so far in March have already taken the base rate to a new all-time low of 0.1% and instigated a new asset purchases programme, which accompanies a new quantitative easing programme in the eurozone (page 4).

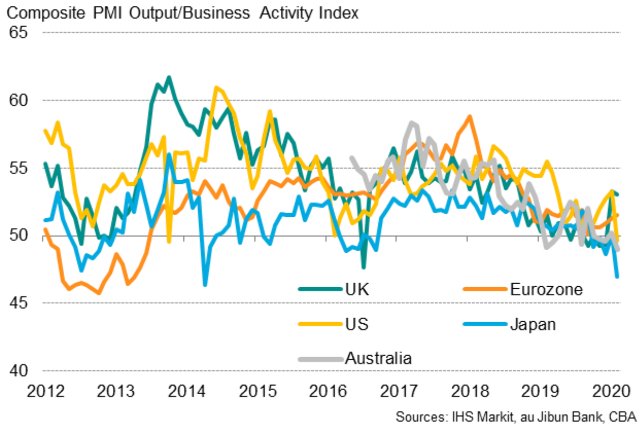
In Asia, expectations of a weak set of PMI data for Japan would cement fears of the economy already being in recession after the contraction seen late last year due to the sales tax hike, while Australia's PMI will be eyed for the impact of travel restrictions on tourism in particular (page 5). Elsewhere, a focus is likely to remain on the recent US dollar's rise, notably in emerging markets with high dollar debt servicing burdens.

Special reports

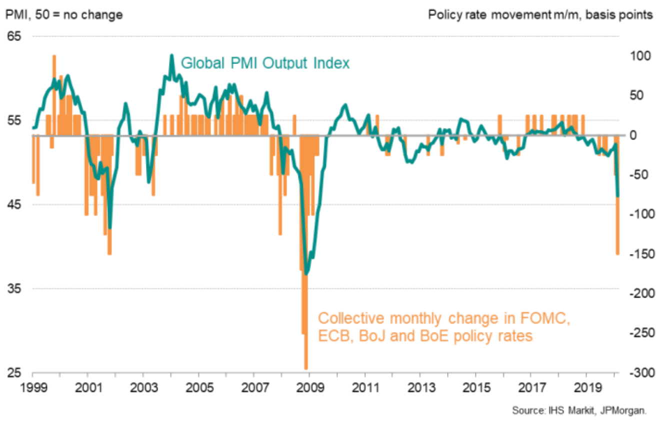
China: We investigate how COVID-19 is driving a deteriorating credit outlook and rising default risk for China's corporate sector. (page 6).

Eurozone: An exceptionally large contraction in eurozone GDP is likely in 2020 given the widespread economic and financial fall-out from the COVID-19 outbreak. (page 9)

IHS Markit's flash PMI surveys for March will provide further insight into the economic impact of COVID-19



Central banks have responded to the signs of economic stress with stimulus measures, with a global recession now being widely forecast.



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Economic Preview: Week of 23 March 2020

Publish date: 20 March 2020

Key diary events (UTC)

Monday 23 March

UK Household Finance Index (Mar)
Thailand trade, new car sales (Feb)
Singapore inflation (Feb)
Taiwan industrial output, retail sales, jobless rate (Feb)
US Chicago Fed national activity index (Feb)
CBA Australia flash PMI (Mar)

Tuesday 24 March

Flash PMI for Japan, US, Eurozone, UK, Germany and France (Mar)
Brazil retail sales (Jan)
US new home sales (Feb), Richmond Fed manufacturing index (Mar)
New Zealand (Feb)
BoJ monetary policy meeting minutes (20-21 Jan)

Wednesday 25 March

RBNZ press conference
Malaysia inflation (Feb)
Thailand monetary policy decision (Mar), industrial output (Feb)
Netherlands GDP (Final, Q4)
UK inflation (Feb)
France jobless benefit claims (Feb)
US durable goods orders (Feb)

Thursday 26 March

Singapore industrial production (Feb)
Hong Kong trade (Feb)
France business confidence (Mar)
UK retail sales (Feb)
Bank of England monetary policy meeting
US GDP (Final, Q4), goods trade balance (Adv, Feb)
US wholesale inventories (Adv, Feb)
Mexico interest rate decision
South Korea consumer confidence (Mar)

Friday 27 March

Thailand unemployment rate (Feb)
China industrial profits (YTD, Feb)
Taiwan consumer confidence (Mar)
UK nationwide house prices (Mar)
Italy business and consumer confidence (Mar)
US personal income, personal spending, PCE (Feb)
US Michigan consumer surveys (Final, Mar)

Sat-Sun 28 – 29 Mar

29/3: Vietnam GDP (Q1), industrial output, trade, retail sales, tourist arrivals, inflation (Mar)
29/3: BoJ summary of opinions (18-19 Mar)

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United States Week Ahead

Flash PMIs, PCE prices and durable goods

By Siân Jones

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Analysts seeking to grasp the extent of the COVID-19 impact on the US economy will be eyeing the release of flash PMIs, which will give the earliest indication of how businesses managed through March as the virus outbreak escalated. Consumer sentiment data are also updated for March by the University of Michigan. Meanwhile, inflation and durable goods orders, personal consumption, new home sales, trade and inventories data for February are published alongside the final estimate of GDP in the final quarter of 2019.

Flash PMIs

March has seen the largest escalation in the outbreak of COVID-19 across the US to date, with cases in every state. The constantly evolving news cycle with regards to government advice and policy, is also searching for signs of how businesses are faring in such uncertain times. Alongside consumer sentiment survey data, the release of the 'flash' PMI for March will indicate how the private sector is performing and give an insight into the extent of the disruptions to business.

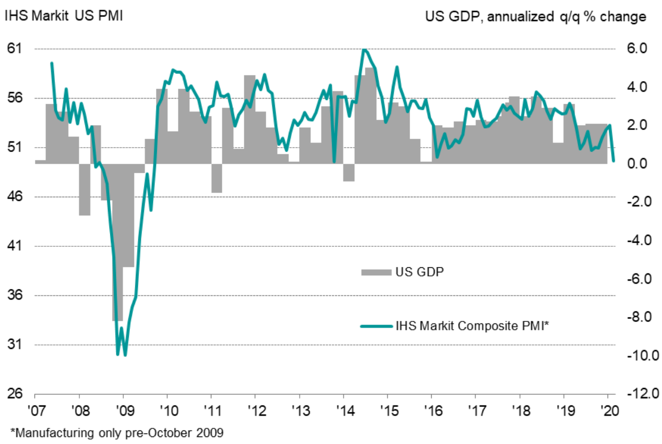
The service sector was already showing signs of strain in February following reduced demand for tourism-related industries in particular. Widespread lockdowns across Europe and travel bans announced in the US may only serve to have exacerbated these challenging demand conditions across both the manufacturing and service sectors in March, with many closing their doors and asking staff to work from home where possible.

Updates to regional surveys including the Chicago Fed National Activity Index, Richmond and Kansas Fed manufacturing indexes are also released.

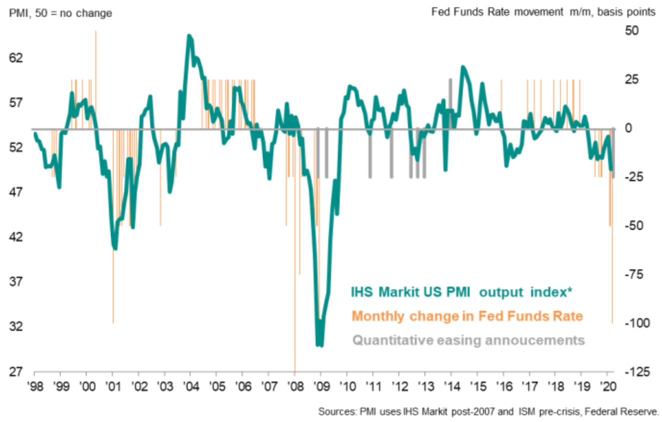
PCE Prices Index

Meanwhile, the rate of PCE price inflation is expected to have remained below 2% in February, although expectations data suggest consumers are forecasting an acceleration in the coming months amid fears of shortages. The pace of core inflation (excluding volatile items such as food and fuel) also looks to be little changed. That said, policymakers' eyes will be moving away from inflation releases for the moment amid global stock market volatility.

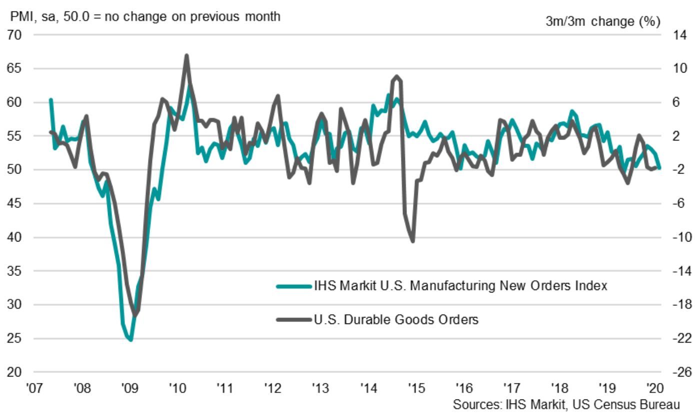
US business performance languishes in difficulties amid a COVID-19 related drop in demand



The Fed has already taken aggressive action to counter the impact of the coronavirus



Manufacturing demand conditions struggle to turn positive, and look set to deteriorate further



Europe Week Ahead

Flash PMIs, Bank of England, consumer confidence surveys

By Joe Hayes

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European flash PMIs will provide a timely insight into the immediate impact of self-isolation and nationwide lockdowns in response to COVID-19 across both the Eurozone and UK, with recessions seemingly an inevitable outcome. Consumer sentiment surveys are also due, as well as retail sales data for February in Germany and the UK. Andrew Bailey will lead his first scheduled Monetary Policy Committee (MPC) meeting as governor, having already overseen two emergency meetings which have taken interest rates to a record low and started new asset purchases.

Bank of England and ECB

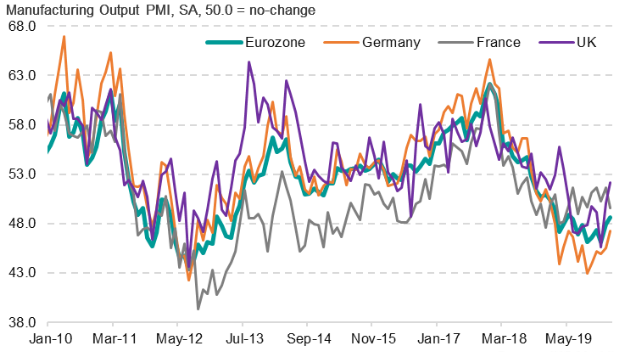
As the COVID-19 outbreak continues to escalate, further action by European central banks and governments cannot be ruled out, especially as financial conditions tighten. In addition to various fiscal measures to help businesses through short-term cash flow stress, the ECB has so far announced €750bn of new asset purchases, with a further £200bn instigated by the Bank of England, the latter having also cut its policy rate to an historic low of 0.1% and brought in targeted loans for SMEs. However, the Bank of England's policymakers meet again in the coming week, armed with fresh economic data in the form of the flash PMIs and consumer confidence data.

Flash PMIs and household finances

With governments imposing nationwide lockdowns, travel bans and, in some cases, draconian measures to limit the spread of COVID-19, flash PMI survey data will help ascertain the immediate effect on business. While February PMI data had shown greater resilience in Europe than seen in Asia and, to some extent, the US, the disruption from the virus in Europe remained primarily to the supply side, meaning March data are likely to include a greater indication of the demand-side impact. While the UK has lagged countries such as Italy, Spain France and Germany in implementing measures to control the virus spread, it is clear that all nations are seeing widespread – if not unprecedented – disruptions across manufacturing and services.

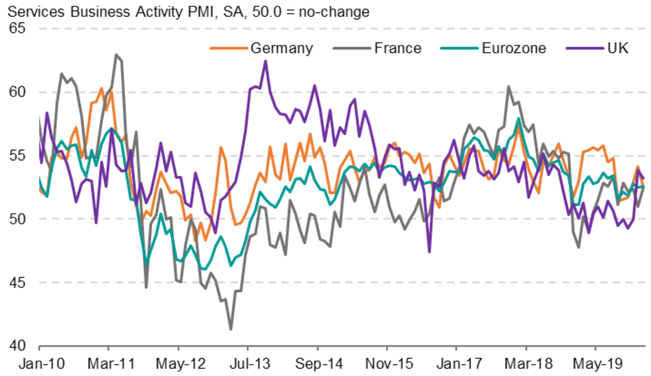
Elsewhere, UK and Germany retail sales data for February are due, as is UK inflation and the IHS Markit Household Finance Index.

Manufacturing PMIs for March to reveal depth of COVID-19 disruption as demand-side shock added to the supply-side impact seen in February



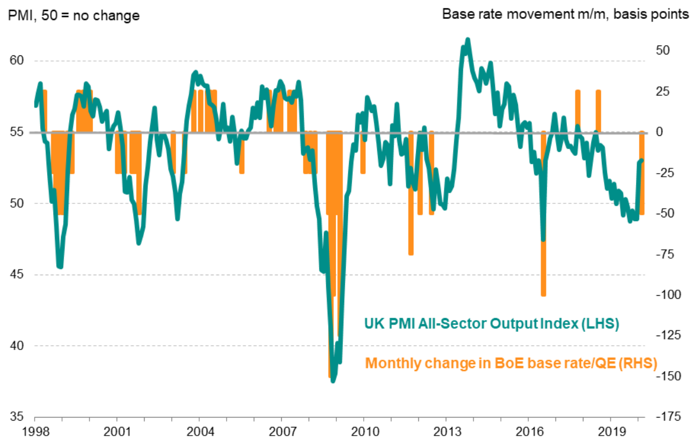
Source: IHS Markit

Imposed lockdowns have heavily disrupted service providers across Europe in March



Source: IHS Markit

Bank of England will need to turn to unconventional policy as interest rates approach the zero lower bound



Sources: IHS Markit, Bank of England.£25bn QE shown as equivalent to 25 basis points

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Asia Pacific Week Ahead

Flash PMI eyed for clues of future policy action

By Bernard Aw

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Flash PMI surveys will provide one of the earliest insights into economic activity during March where increasingly severe measures were taken around the world to contain the spread of COVID-19. In Asia, expectations of weak PMI results for Japan and Australia will raise calls for more policy support. Central bank policy action is meanwhile scheduled to come from the Bank of Thailand. Investors will also monitor the Bank of Japan's summary of opinions for the March meeting.

Other data highlights in Asia include trade numbers in Thailand and Hong Kong SAR, along with industrial output data in Singapore, Taiwan and Thailand, as well as China's industrial profits. Vietnam will publish first quarter GDP figures.

Flash PMI for Japan and Australia

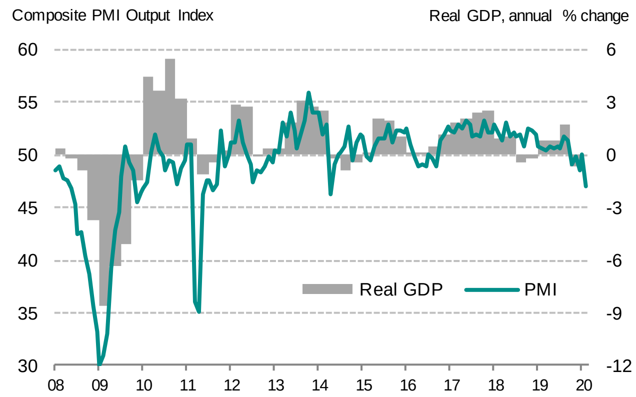
March flash Jibun Bank PMI for Japan will be scrutinised for signs that the economy has fallen into recession after the contraction already seen in the fourth quarter of last year, when activity was dampened by typhoon-related disruptions and the sales tax hike. Recent PMI surveys showed that measures taken to limit the spread of COVID-19 has severely impacted the tourism sector and manufacturing industry across Japan.

In Australia, analysts will parse the flash PMI results for likely signs of increasing recession risks, thereby providing further clues as to whether greater policy interventions, particularly fiscal measures, are needed to offset the impact from the COVID-19 outbreak.

Bank of Thailand

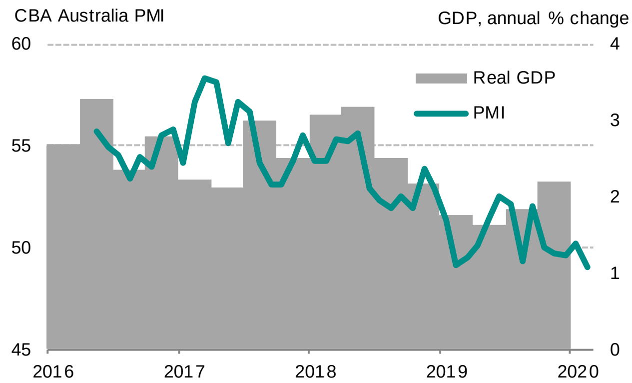
The Thai central bank convenes to decide on monetary policy in an environment of slowing growth and increasing risks to the economy brought about by the global spread of the COVID-19 virus, exacerbated by local drought conditions. With the pandemic affecting trade and tourism, the worsening growth prospects for Thailand raise expectations of further monetary support from the central bank. However, monetary policymakers will also take into account the recent depreciation of the Baht when mulling over any decisions to cut policy rates further.

Recent Japan PMI data point to deepening recession amid COVID-19 outbreak



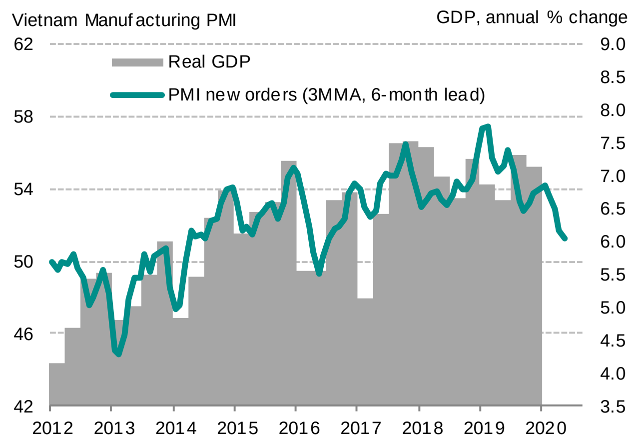
Sources: IHS Markit, au Jibun Bank, Cabinet Office

Australia PMI and economic growth



Sources: IHS Markit, CBA, ABS

Vietnam PMI signal slowing GDP growth



Sources: IHS Markit, General Statistics Office of Vietnam

Asia Pacific Special Focus

China: COVID-19 drives deteriorating credit outlook and rising default risk for China's corporate sector

By Zerlina Zeng

APAC Lead, Credit Risk Assessment, IHS Markit

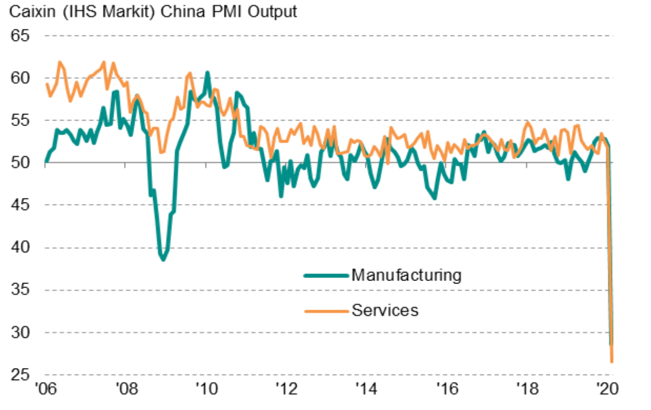
We believe the credit outlook for Chinese corporates has deteriorated amid the coronavirus disease 2019 (COVID-19) pandemic. Default risk is elevated for corporates with strained liquidity and high reliance on short-term debt, including small-to-medium sized private corporates (SMEs) and local state-owned enterprises (SOEs) backed by weak district governments. However, we do not foresee large scale corporate default as monetary and fiscal support has been strong, bond refinance is speeding up, and banks are rolling over overdue loans. Nevertheless, outright bailout of corporates and local SOEs is unlikely given the weakening fiscal stance and elevated debt burden of Chinese local governments.

COVID-19 impact on industry sectors

Since the outbreak of COVID-19 in China in January, sectors that rely on discretionary consumer spending and manufacturers with global supply chains have experienced a direct negative impact. These include corporates in retail, hospitality and gaming industries, as well as transportation operators and manufacturers of autos and electronic goods. As the impact of COVID-19 prolongs into March, industrial sectors with high fixed costs and those reliant on monthly operating cashflow to pay for debt servicing are facing rising pressure. These include metals & mining, engineering & construction and property developers.

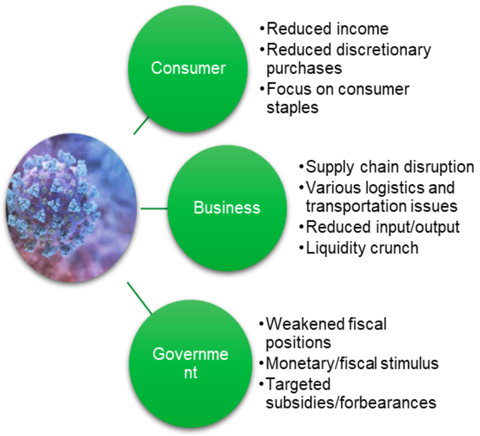
While business operations and production are showing signs of gradual resumption, high frequency data, such as daily coal production and property sales, indicate that activity levels are still extremely low. We estimate that if measures to contain the spread of COVID-19 prolong into the second half of the year, all sectors including the defensive utilities, healthcare, telecom and business services will feel the pain. An increasing number of corporates could deplete their cash reserves and default, which in turn could result in rising problem loans on balance sheets of Chinese commercial banks.

Caixin Mainland China PMI



Source: IHS Markit, Caixin.

Impact of COVID-19 on consumers, business and government



Source: IHS Markit Economic & Country Risk, IHS Markit Industry Research.

Corporates rely on consumer discretionary spending and global supply chain will feel the most pain

Auto	Very high
Gaming	Very high
Hospitality	Very high
Retail	Very high
Technology	Very high
Transportation	Very high
Banks	High
Engineering & construction	High
Metals & mining	High
Oil & gas	High
Property	High
Insurance	Medium
Utilities	Medium
Business services	Low
Healthcare	Low
Telecom & Media	Low

Source: IHS Markit Economic & Country Risk, IHS Markit Industry Research.

Economic Preview: Week of 23 March 2020

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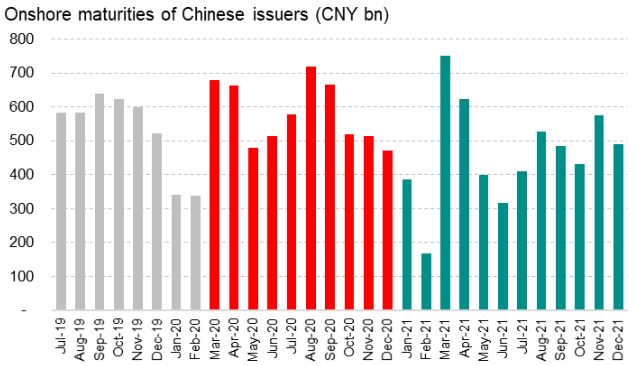
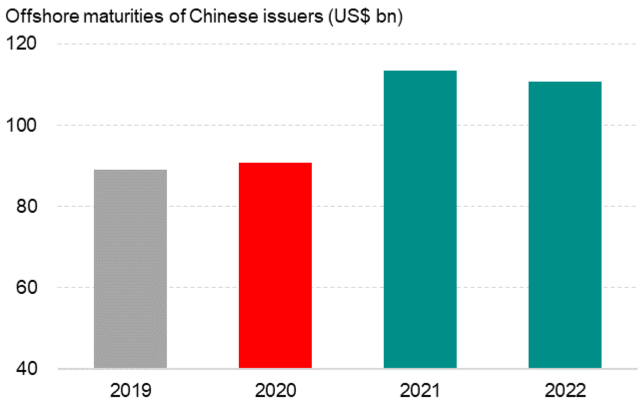
Even before the outbreak of COVID-19, 2020 was set to be a tough year for Chinese issuers due to large bond maturities, including over CNY 6 trillion onshore and around USD 90 billion offshore. We believe Chinese issuers' liquidity was already weak before the virus outbreak. We assess a company's liquidity position by dividing its cash and unused credit line over its next 12-month debt service period, and by looking at its cashflow coverage of interest. We observe that the majority of Chinese issuers have limited headroom to buffer prolonged operation disruption due to COVID-19. In addition, utilisation of longer-dated bonds or loans is limited, indicating heightened refinance risk.

Onshore bond maturities of Chinese issuers



Sources: China Bond, Factset, IHS Markit.

Offshore bond maturities of Chinese issuers



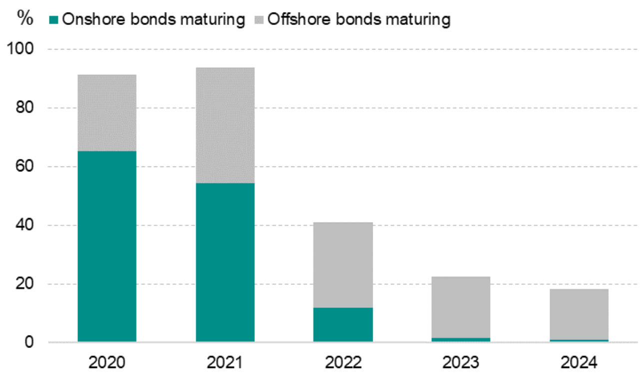
Sources: China Bond, Factset, IHS Markit.

Moreover, it is worth noting that there has been a clear "flight to quality" since 2019. In May 2019, the government took over Baoshang Bank, resulting in widespread funding stress. Since then, private companies have been crowded out by SOEs in financing channels including the bond market. As a result, bond default rate was substantially higher for private companies in 2019. Such trends are likely to continue in 2020.

Chinese property issuers are the bellwether of the Asian high-yield bond market. For property developers, the closedown of property sales centres nationwide has impacted contracted sales. Halted property construction has caused delayed deliveries and revenue recognition. For retail sector landlords, the slump in pedestrian traffic puts downward pressure on occupancy rates and lease rates.

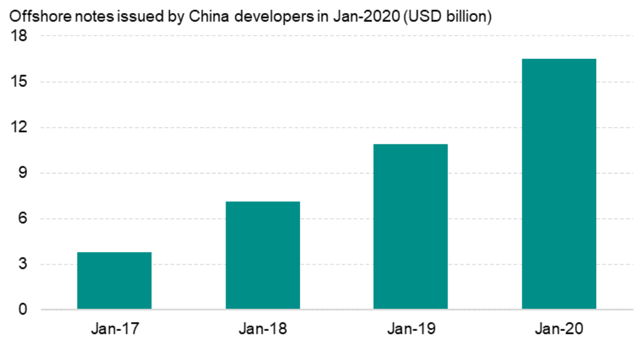
As of now, the impact is still manageable for medium-to-large sized developers. Wuhan and Hubei Province, the epicentre of COVID-19, account for a small portion of the nation's total real estate investment and residential property sales. The first quarter of the year is low season for home sales, with January and February contributing to less than 7% of annual sales on average in the past 10 years. Developers are also using online sales and virtual tours of new homes to mitigate the closure of sales centres. In addition, we also expect government policy measures to be supportive. Since late January, various local governments have announced supply-side measures to ease developers' liquidity pressure such as deferring land premium payment and lowering presale threshold.

Chinese property developers face large maturities in 2020



Sources: China Bond, Factset, IHS Markit.

Property developers obtained large refinance ahead of COVID-19 outbreak



Sources: China Bond, Factset, IHS Markit.

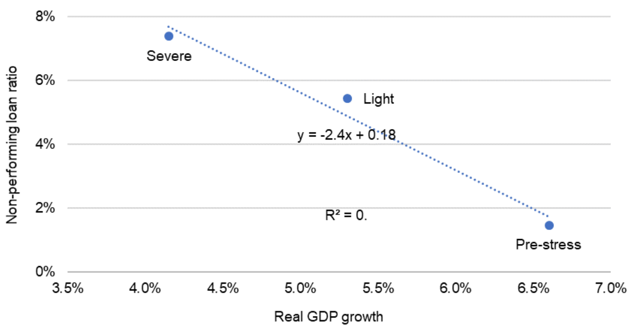
Chinese property developers have hefty onshore and offshore maturities in 2020. However, they obtained large refinancing ahead of the COVID-19 outbreak. In January, they issued in aggregation USD 16 billion offshore dollar bonds, doubling the amount issued in January 2019. This helps to alleviate their refinance pressure for the rest of the year.

However, small regional players are already feeling the liquidity squeeze, and some have been forced to default or undertake debt restructuring. If COVID-19 cases should resurge in the second and third quarters, where most sales activity happens, the Chinese property sector could face price declines and a sharp slowdown in housing construction. Demand-side stimulus, such as relaxation of purchase restrictions and mortgage terms could have limited impact as Chinese household leverage has increased in recent years.

The impact of COVID-19 on China's banking sectors are from multiple sources. The rising number of distressed corporates could result in surging problem loans, impairing banks' balance sheets and capital adequacy. Banks are particularly exposed to the credit stance of property developers through construction loans and home mortgages. Banks are also the largest holder of bonds issued by Chinese local governments, whose fiscal stance and credit worthiness are deteriorating. Furthermore, a large portion of trust and wealth management products structured through shadow banking are channelled to local government financing platforms and the property sector.

The stress test conducted by China's central bank, the Peoples' Bank of China, (PBOC) in its 2019 financial stability report reveals that China's banking non-performing loan ratio is highly correlated with real GDP growth. The PBOC tested 30 banks, which represent more than 85% of China's banking assets. The stress test found that the banking sector could see their aggregated non-performing loan ratio rise to 5.4% (YE2019: 1.89%; end of Feb-2020: 2.08%) should real GDP growth slow to 5.3%. Under the severe scenario, where real GDP growth drops to 4.2%, the non-performing loan ratio could shoot up to 7.4%, the non-performing loan balance would reach 10% of GDP, and multiple banks would fail various regulatory capital requirements. However, with the risk that a bank failure or forced take-over could threaten funding for banks and increase liquidity pressure, it is likely that the authorities will prevent systemic risks to the sector by ensuring the sector's structure remain largely unchanged.

Non-performing loan ratio of 30 Chinese banks under stress test given real GDP growth assumptions



Source: PBoC Financial Stability Report, IHS Markit.

To ensure stability of the financial system, Chinese banks have been guided by the central government to provide support to borrowers. This includes extending loan maturities for corporates in COVID-19 affected industries and regions. Moreover, the government is expected to relax the recognition of non-performing loans, and to extend the transition period of the asset management new rules that target to curb shadow banking. Such measures could give distressed Chinese corporates some breathing room but would likely delay the banking reform initiatives carried out in recent years.

Credit outlook

The escalation of the COVID-19 crisis outside China has increased the likelihood of a global recession. Market volatility will likely remain high amid weak investor sentiment, and policy actions will continue to dominate asset performance including credit markets. Although China's domestic corporate bond spreads have tightened against stable onshore risk sentiment, we believe credit risk in China's corporate sector remains elevated and the outlook would likely deteriorate due to spill-over effects from a global growth slowdown. We expect corporates with limited liquidity headroom and high reliance on short-term finance to face heightened default risk. We also expect episodes of local SOE default, which started in late 2019, to increase due to the weakening credit stance of local Chinese governments.

Europe
Special Focus

Eurozone: COVID-19 shock to drive the eurozone into severe recession, tail risks in focus

By Ken Wattret

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An exceptionally large contraction in eurozone GDP is likely in 2020 given the widespread economic and financial fall-out from the COVID-19 outbreaks.

The consequences for Italy in particular, and the eurozone more broadly, could go well beyond the short-term impact on economic growth. Risks surrounding debt sustainability and deflation are back in the spotlight.

Recession unavoidable, just a question of how severe

In our initial response to the coronavirus outbreak in China and potential spillovers to Europe back in February, we concluded that a Europe-wide recession would require widespread contagion of the COVID-19 virus beyond China's borders. Unfortunately, this is precisely what has been happening since. Accordingly, we have slashed our 2020 GDP forecasts across Europe.

In the eurozone, we now forecast an annual contraction in GDP of around 1.5% in 2020, based on three consecutive q/q declines from Q1 to Q3 2020. The magnitude of the output losses reflects the broad-based nature of the shock, including:

- Collapsing exports and industrial production due to severe reductions in demand and extensive disruption to supply chains across the globe.

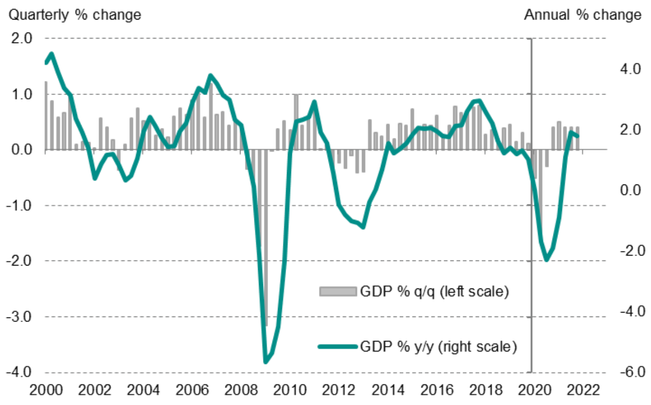
- Plunging consumer spending and services activity, with areas such as retail stores, restaurants, hotels, entertainment and transportation to suffer extreme disruption, compounded by weaker consumer sentiment, employment losses and higher precautionary saving.

- Weaker investment due to huge uncertainty and tighter financial conditions, including collapsing equity markets, rising risk premia and possible credit constraints.

How bad could it be?

As Chart 1 shows, our baseline forecast now includes sizeable q/q contractions in eurozone GDP in Q1 and Q3 2020 and an exceptionally large fall in Q2 (around 1.5% q/q), which we currently assume will be the peak decline. The output losses are forecast to be deeper and faster than during the eurozone crisis in 2011-12, as Chart 1 illustrates. But the forecast decline for Q2 is still a long way short of the peak q/q decline at the height of the Global Financial Crisis (GFC) in Q1 2009 (3.2% q/q). So too the expected cumulative fall in GDP in 2020 relative to the GFC (less than half of the near six percentage point drop in 2008-9). This implies that there are significant downside risks to our projections.

Chart 1: Eurozone recession looms



Source: Eurostat, IHS Markit

The duration of the current downturn (three quarters) is also forecast to be shorter than the GFC (five quarters) and the eurozone crisis (six quarters), reflecting the different nature of the shocks. The more radical the containment measures introduced in the current period, the bigger the near-term economic damage but hopefully the more likely successful containment of the spread of the virus becomes, allowing a subsequent upturn. It could still take much longer than we assume to return to positive growth, however, again suggesting risks are very much to the downside.

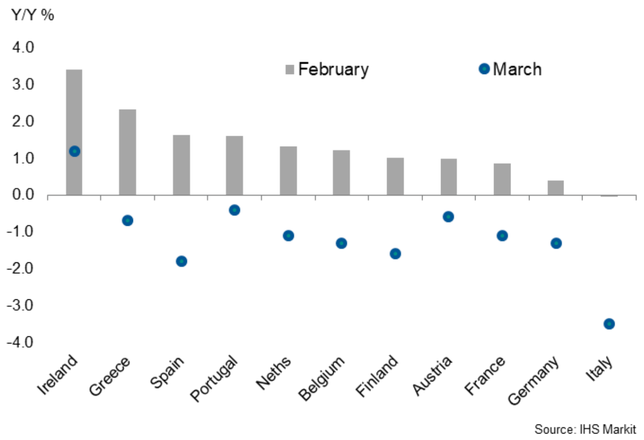
In our baseline we assume that there will only be a partial, not fully offsetting, rebound in economic activity in the eurozone once the most acute phase of disruption and uncertainty has eased, which we assume from Q4 2020. For many areas of the service sector particularly, activity that was lost will not be recouped subsequently. It could also take quite some time for behaviour to return to normal, even after extreme containment measures have been removed and the spread of the virus has ceased, as cautious consumers are reluctant to venture back out.

We acknowledge the huge uncertainty surrounding these forecasts. The rates of contraction in the coming quarters could be much larger and longer lasting than we expect and maybe also the subsequent rebound, depending on the effectiveness of the policy responses.

The initial response in Europe was not impressive, from many governments, the EU and the ECB. At the time of writing, this has started to step up but market confidence in policy makers remains low, with the small-scale, piecemeal measures initially announced in Europe worryingly reminiscent of the multiple policy failures during the GFC and the subsequent eurozone crisis.

As we see it, large-scale fiscal stimulus must be at the forefront of the response across member states, but with the full support of EU institutions, including a revamped ECB asset purchase programme. But even with a broader range of more impactful policy measures, severe contractions in output are unavoidable in the period ahead.

Chart 2: Revisions to 2020 GDP forecasts



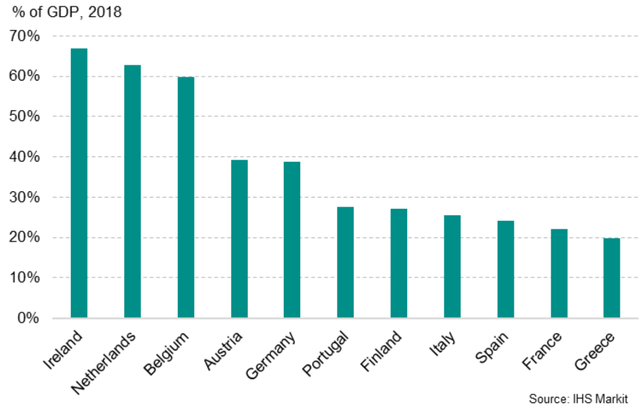
Variations in member states' vulnerability

In our initial response to the shock, we highlighted some of the key differences in eurozone member states' vulnerabilities. These differences are reflected in our forecasts in Chart 2, which show the major revisions we have made for 2020 GDP in the largest eleven member states. Combined, they make up over 95% of eurozone GDP.

Two key metrics are highlighted below, for the largest eleven eurozone member states.

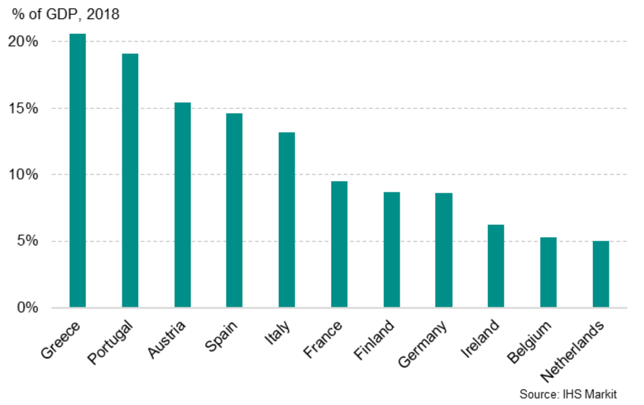
First, openness to trade. Chart 3 shows the exports of goods for each economy relative to GDP, based on 2018 data. A few economies are exceptionally open to trade, including Ireland (the role of multinationals), the Netherlands and Belgium (related to the importance of their key ports). Germany's ratio is not as high but at around 40%, it is well above those in France, Italy and Spain, the other three largest eurozone economies (all below 25%).

Chart 3: Exports of goods



Second, another key vulnerability for Europe, a collapse in tourism. This is a key area of economic activity for southern Europe particularly, including Italy.

Chart 4: Travel & Tourism



Chronic crisis in Italy now risks becoming an acute crisis

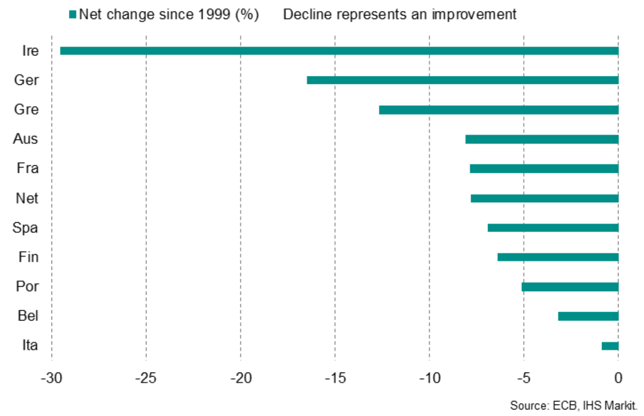
In addition to trying to gauge the magnitude of the drop in GDP, we are also trying to highlight some of the broader risks and consequences, and one of our long-standing concerns has been Italy's perilous fiscal position and its vulnerability to adverse shocks.

Expectations of large additional expenditures to contain the health crisis, tumbling revenues as economic activity collapses, plus concerns about the ineffectiveness of policy responses, including from the ECB, led to a huge widening of Italian sovereign yield spreads versus German benchmarks from late

February. While higher sovereign risk premia have been evident across the eurozone, the shift in Italy was much larger, commensurate with Italy's dep-rooted problems. The recent ramping up of the ECB's asset purchase programme was well received initially but the underlying issues remain.

Since joining the monetary union, Italy has persistently underperformed growth-wise. Nominal exchange rate flexibility was given up but without the flexibility required to maintain competitiveness through internal devaluations (i.e. containment of relative unit labour costs and prices). The result has been large, sustained competitiveness losses against other eurozone member states (Chart 5).

Chart 5: Harmonised competitiveness indicators (unit labour cost basis)

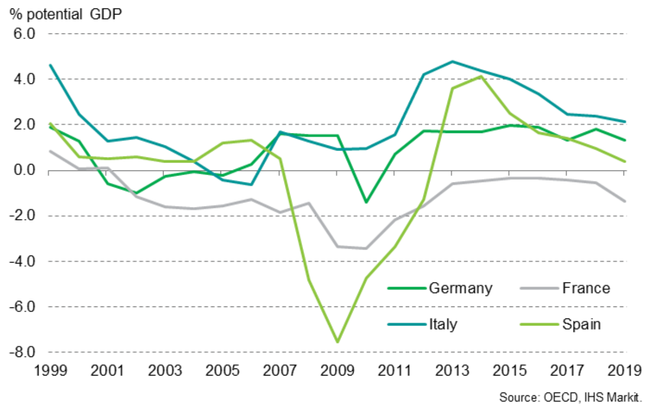


Italy's relatively high public sector debt to GDP ratio has not been falling in recent years either despite improving economic conditions from 2013 onwards and the windfall of low interest rates due to ECB policy accommodation. Nominal growth in Italy is low relative to peers, while the primary budget surplus (excluding interest payments) has fallen significantly in recent years. This is due to discretionary policy adjustments not the disappointing economic performance, shown in the accompanying decline in Italy's cyclically adjusted primary budget surplus (Chart 6). Relative to GDP, Italy's primarily surplus has fallen by around two and a half percentage points since 2013.

This leaves the Italian public sector debt to GDP ratio very vulnerable to sustained rises in interest rates. Hence the extreme market reaction to ECB president Christine Lagarde's comments on 12th March about it not being the ECB's job to bring down yield spreads.

High debt and low growth are not unique to Italy but Italy is a much bigger threat to eurozone stability given its size, which the eurozone's support structures (e.g. the ESM) are not equipped to cope with currently. Add in the vulnerability of Italy's banking sector to rising NPLs, its high exposure to sovereign debt and the Italian government's inability to provide large-scale financial support to banks if needed and the combination of vulnerabilities suggests a very significant risk of a broad-based Italian crisis and potential spillovers elsewhere (including to other banking systems, including France).

Chart 6: Cyclically adjusted primary budget balances



A key indication of the initial severity of the economic impact from the COVID-19 outbreak on the eurozone will be provided by IHS Markit's flash PMIs for March, published 24th March, with data collected 12th-23rd March.