Coronavirus Poses Downside Risk To The Global Economy

In the last couple of weeks, the world has witnessed the outbreak of the Coronavirus (2019-nCov) infection, and its global diffusion. According to the most recent statistics, there are 14,500 people reported as infected in Asia, more than 9000 of whom are in China. The virus has been detected in at least 24 countries. Even then, it is likely that the number of infected people has been under-reported. So far, 305 people have died, with the first victim reported being located outside of China, in the Philippines.

It is understood that the virus originated in Wuhan, a city of 11 million people in central China. It was initially reported that the origin of the virus was the seafood and poultry market in Wuhan. However, the origin remains disputed. A study published on Lancet says that the Wuhan market might not be the origin of the virus. According to some theories (bordering on conspiracy theories), the virus might have originated from a biosafety laboratory – also based in Wuhan – housing some of the world’s most deadly illnesses. The lab, opened after the outbreak of Severe Acute Respiratory Syndrome (SARS) in 2003, is used to study class four pathogens (P4), referring to the most virulent viruses which pose a high risk of “aerosol-transmitted person-to-person infections,” according to a press release. It is possible that we will not be able to establish for certain the origin of this virus, but we cannot exclude a-priori that the virus originated from lab experiments.

 Plenty of comparisons have been made with the SARS episode, which in 2002-03 infected more than 8,000 people, killing around 700 of them. Some studies have also analysed the economic costs of SARS (estimated to be around USD 13bn). According to initial statistics conducted on the first 99 patients at a hospital in Wuhan, the Coronavirus has a case-fatality rate (the percent of deaths among those infected) of 11%. Initial estimates show that the virus has an R0 of 2.2, meaning each case patient could infect more than 2 other people. If those statistic prove accurate, this virus would be more infectious than the 1918 “Spanish-Flu” pandemic virus, which had an R0 of 1.80. Based on current statistics, Coronavirus is definitely more infectious and deadly than SARS, and possibly also than the Spanish Flu of 1918-19, which infected more than half a billion people and killed an estimated 20-50 million (statistics were not very accurate in that case, in part because of World War I). At the same time, to most people’s surprise, the Coronavirus is less severe than the usual seasonal flu. Just to give an example, seasonal influenza epidemics cause 3 to 5 million severe cases and kill up to 650,000 people every year, according to the World Health Organization. So far in this season, there have been an estimated 19 million cases of flu, 180,000 hospitalizations and 10,000 deaths in the US alone, according to the Centers for Disease Control and Prevention.

So, what is making the Coronavirus so special, and worthy of attention, to the point that every major central banker (e.g. Fed’s Powell, Boe’s Carney and ECB’s Lagarde) had to answer a question about its impact? The point is that the panic that the outbreak has created, and the defensive reactions to it, might be causing quite a severe level of damage to the global economy (even if perhaps only temporarily, in which case the losses might be mostly recouped in the following quarters). A number of airline companies have completely interrupted all of their flights in an out from China; British Airways, which has cancelled every flight until March, being only a very notable example of this. Most importantly, the US has barred entrance to any foreigner travelling from mainland China. A number of other countries, such as Australia, have followed the US’ example. China has reacted with anger to the measures adopted by the US and other countries. China risks being isolated by the rest of the world, a position that is politically and economically difficult for Beijing to tolerate, especially as the trade and tech negotiations with the US are still ongoing, following the Phase-1 deal between the two countries.

So, more than the virus per se, it is the various countries’ reactions to the virus which pose serious downside risks to the global economy. Indeed, the global economy risks another year of stagnation, following a disappointing 2019. If that happens, central banks and fiscal authorities will likely have to do their part to support aggregate demand in the various countries directly or indirectly hit by the outbreak.

Our Recent Publications

- Flash Preview: RBA To Hold Off Providing Further Easing (For Now), By Brunello Rosa and Karmen Meneses, 31 January 2020
- Bank of England Flash Review: “So Far Good Enough,” But A Rate Cut Remains On The Table, By Brunello Rosa, 30 January 2020
- Flash Preview: Fed to Remain on Hold in January, By N. Roubini, Brunello Rosa and Alessandro Magnoli Bocchi, 27 January 2020
- Flash Review: Regional Elections Give a Breather To The Italian Government, By Brunello Rosa, 27 January 2020

GEOPOLITICAL CORNER: The Olympian View: Mapping The Global Strategic Topography, By J. C. Hulsman, 28 January 2020
Looking Ahead

The Week Ahead: US Senate Blocks A Call For New Witnesses In The Impeachment

In the US, the Senate blocked a call for new witnesses into the Presidential impeachment case. As a result, the final vote will take place on February 5 and the Senate will likely acquit Mr. Trump.

In the US, January’s labour market data is expected to indicate: i) a pick-up in non-farm payrolls (c: 165k; p: 145k); ii) acceleration in earnings (Avg. hourly earnings: c: 3.0% y-o-y; p: 2.9); and iii) still low unemployment (c: 3.5%; p: 3.5).

In Australia, the RBA will likely remain on hold (c: 0.75%; p: 0.75).

In Turkey, inflation will likely remain in double-digits (c: 11.8% y-o-y; p: 11.8).

The Quarter Ahead: Coronavirus Threatens Growth Prospects

The WHO declared the coronavirus a ‘global public-health emergency’, as the number of confirmed cases exceeded the total of the 2003 SARS epidemic. According to the WHO, the virus outbreak could expand beyond China; however, for now, ‘there is no need for measures that interfere with travel and trade’. Several international airlines suspended flights to and from China and international businesses shut down their operations.

In the US, Chair Powell stated that the Fed is: i) ‘yet to see a decisive recovery in the manufacturing sector’, which has weighed on domestic growth; and ii) unlikely to change its policy rate unless ‘the economic outlook materially changes. Yet, the market probability of ‘one or more’ rate cut increased to 88.5% (p: 67.8).

As the UK formally left the EU, the BoE revised down its growth projections for the next three years; yet, all current trading agreements will remain unchanged until the end of 2020. According to BoE governor Mark Carney economic data are ‘good enough’, but a ‘pick-up in economic activity is needed’ to avoid a rate cut in the future.

In China, in Q1-2020: 1) the lockdown of several cities will negatively impact sales, tourism, and transport; and 2) the three-day extension of the lunar new year holiday will further reduce economic growth.

Last Week’s Review

Real Economy: Economic Growth Prospects Weaken, DM Central Banks Stay ‘On Hold’

In the US, in Q4-2019 the economy expanded at 2.1% on a yearly basis (y-o-y), as expected (c: 2.1; p: 2.1); yet, on a quarterly basis (q-o-q) GDP growth slowed to 1.5%, below-consensus (c: 1.8; p: 1.7) - as softer spending and restrained business investment weighed on economic activity. For 2019 in total, growth expanded by 2.3% (p: 2.9), missing the Trump administration’s goal of 3% annual growth.

In December, the Congress’ approval to boost military spending increased ‘defence orders’ and supported a rise in ‘overall durable goods orders’ (a: 2.4% m-o-m; c: 0.4; p: -3.1); yet, ‘durable goods orders excluding defence’ - a proxy for business investment - fell sharply, below-consensus (a: -2.5% m-o-m; c: 0.5; p: -0.5). Headline and core readings of inflation rose (Core PCE Dec., a: 1.6% y-o-y; c:1.6; p:1.5; PCE, a:1.6% y-o-y; p: 1.4). As widely expected, the Fed kept the Fed funds target unchanged, between 1.50-1.75%.

In the EZ, the slowdown was greater than anticipated, as the bloc suffered its weakest quarterly growth since 2012 (a: 0.1% q-o-q; c: 0.2; p: 0.3; GDP Q4, a: 1.0% y-o-y; c: 1.1; p: 1.2). Core inflation slowed to 1.1% y-o-y, further away from the ECB’s target (Jan., c: 1.2%; p: 1.3), while the headline reading rose as expected 1.4% (c: 1.4; p: 1.3).

In the UK, the BoE maintained its key rate at 0.75%, as committee members voted 7:2 in favour of holding rates – in line with the December vote.

Financial Markets: Uncertainty Over Economic Impact Of Coronavirus Hinders Markets

Market drivers: As the coronavirus outbreak threatens to hurt already-fragile growth prospects, investors sought haven assets. In China, the financial markets were closed due to the lunar new year holiday.

Stocks: w-o-w, global indices fell (MSCI ACWI, -2.6% to 559), driven by DMs (S&P 500, -2.1% to 3,226; Eurostoxx 50, -3.7% to 3,641). Volatility rose (VIX S&P 500, +4.2 pts to 18.8; 52w avg.: 14.8; 10y avg.: 16.7).

Bonds: w-o-w, returns rose (BAML Global, +0.7% to 289.8), driven by ‘risk-off’ sentiment, and yields fell across DMs (10y UST, -16 bps to 1.52%; 10y German bund, -11 bps to -0.44%). The US yield curve inverted, as the yield on 10y USTs fell below the yield of 3m bills. FX: w-o-w, the USD fell against a basket of currencies (DXY, -0.5% to 97.390) while the EUR and GBP strengthened (EUR/USD, +0.6% to 1.109; GBP/US, +0.9% to 1.320). EM currencies declined (MSCI EM Currency, -0.9% to 1,647).

Commodities: Amid concerns that the coronavirus outbreak will weaken oil demand, Opec is considering an earlier meeting to further reduce economic growth.

For more information, please call us on +44 (0)207 1010 718 or send us an email to info@rosa-roubini-associates.com

www.rosa-roubini-associates.com
118 Pall Mall, London SW1Y 5ED

Farah Aladsani contributed to this ViewSletter.

The picture in the front page comes from this website
Disclaimer: All material presented in this report is provided by Rosa & Roubini Associates-Limited for informational purposes only and is not to be used or considered as an offer or a solicitation to sell or to buy, or subscribe for securities, investment products or other financial instruments. Rosa & Roubini Associates Limited does not conduct “investment research” as defined in the FCA Conduct of Business Sourcebook (COBS) section 12 nor does it provide “advice about securities” as defined in the Regulation of Investment Advisors by the U.S. SEC. Rosa & Roubini Associates Limited is not regulated by the FCA, SEC or by any other regulatory body. Nothing in this report shall be deemed to constitute financial or other professional advice in any way, and under no circumstances shall we be liable for any direct or indirect losses, costs or expenses nor for any loss of profit that results from the content of this report or any material in it or website links or references embedded within it. The price and value of financial instruments, securities and investment products referred to in this research and the income from them may fluctuate. Past performance and forecasts should not be treated as a reliable guide of future performance or results; future returns are not guaranteed; and a loss of original capital may occur. This research is based on current public information that Rosa & Roubini Associates considers reliable, but we do not represent it is accurate or complete, and it should not be relied on as such. Rosa & Roubini Associates, its contributors, partners and employees make no representation about the completeness or accuracy of the data, calculations, information or opinions contained herein or by personal or client relationships. We also certify that no part of our compensation was, is or will be, directly or indirectly, related to the views expressed in this report.