

GLOBAL ECONOMIC OUTLOOK

Coronavirus outbreak represents binary risk for the global economy

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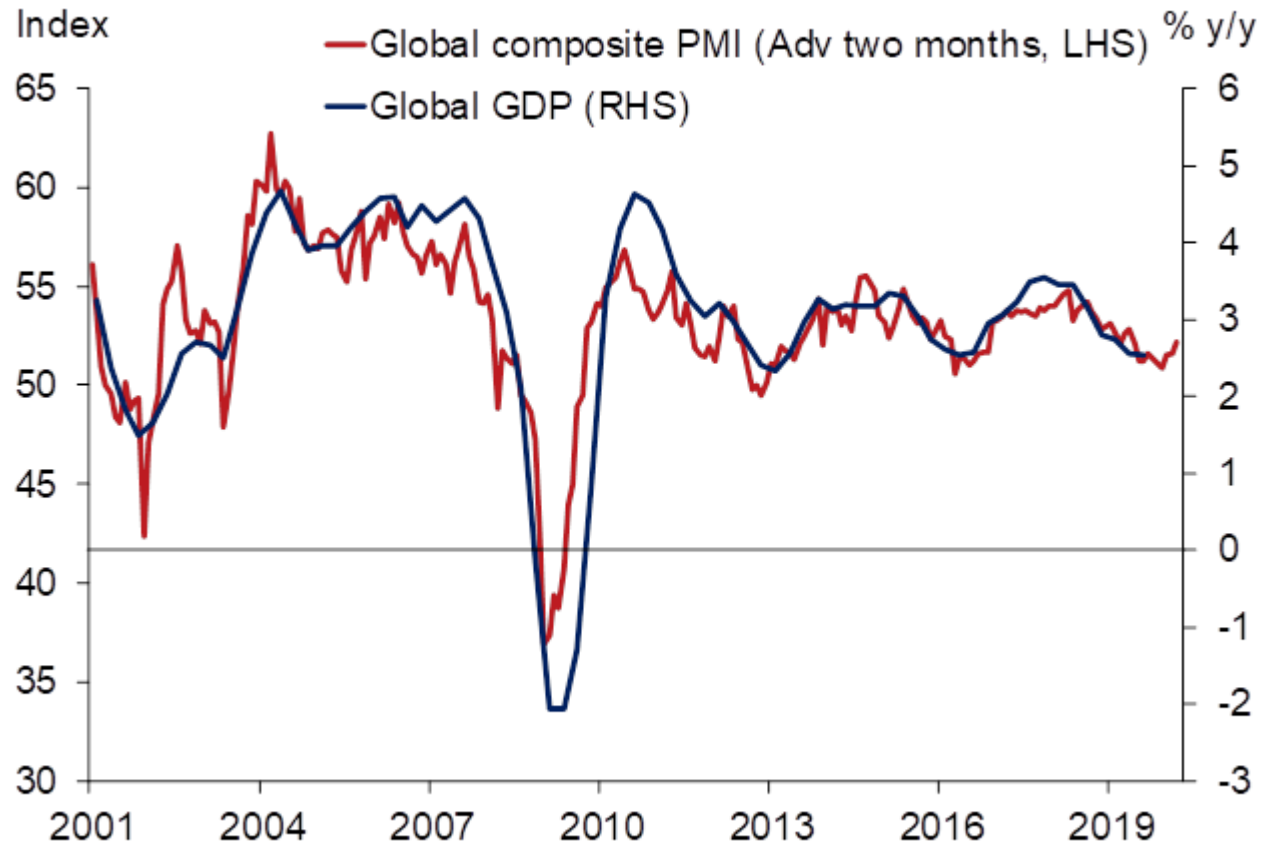
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4 March 2020

Global activity recently showing signs of bottoming out

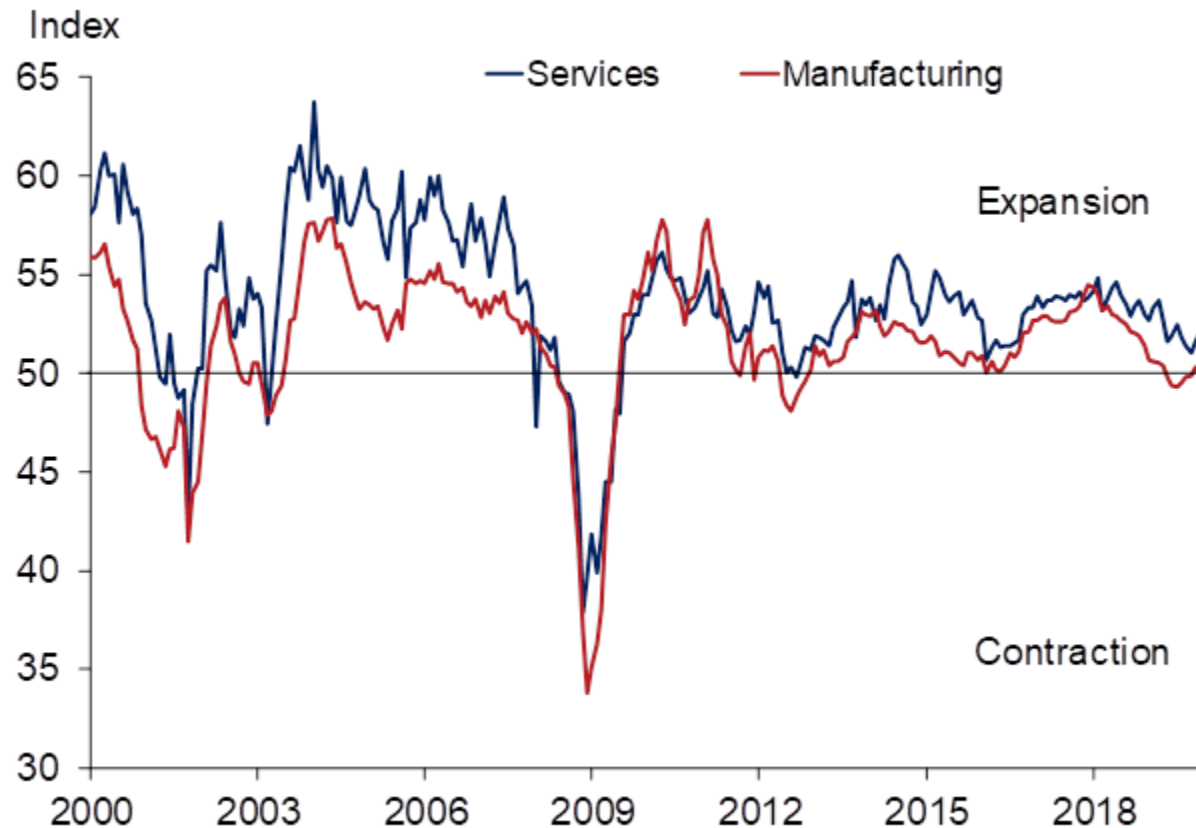
World: GDP & PMI



Source : Oxford Economics/Haver Analytics/Markit

With encouraging leading indicators, until...

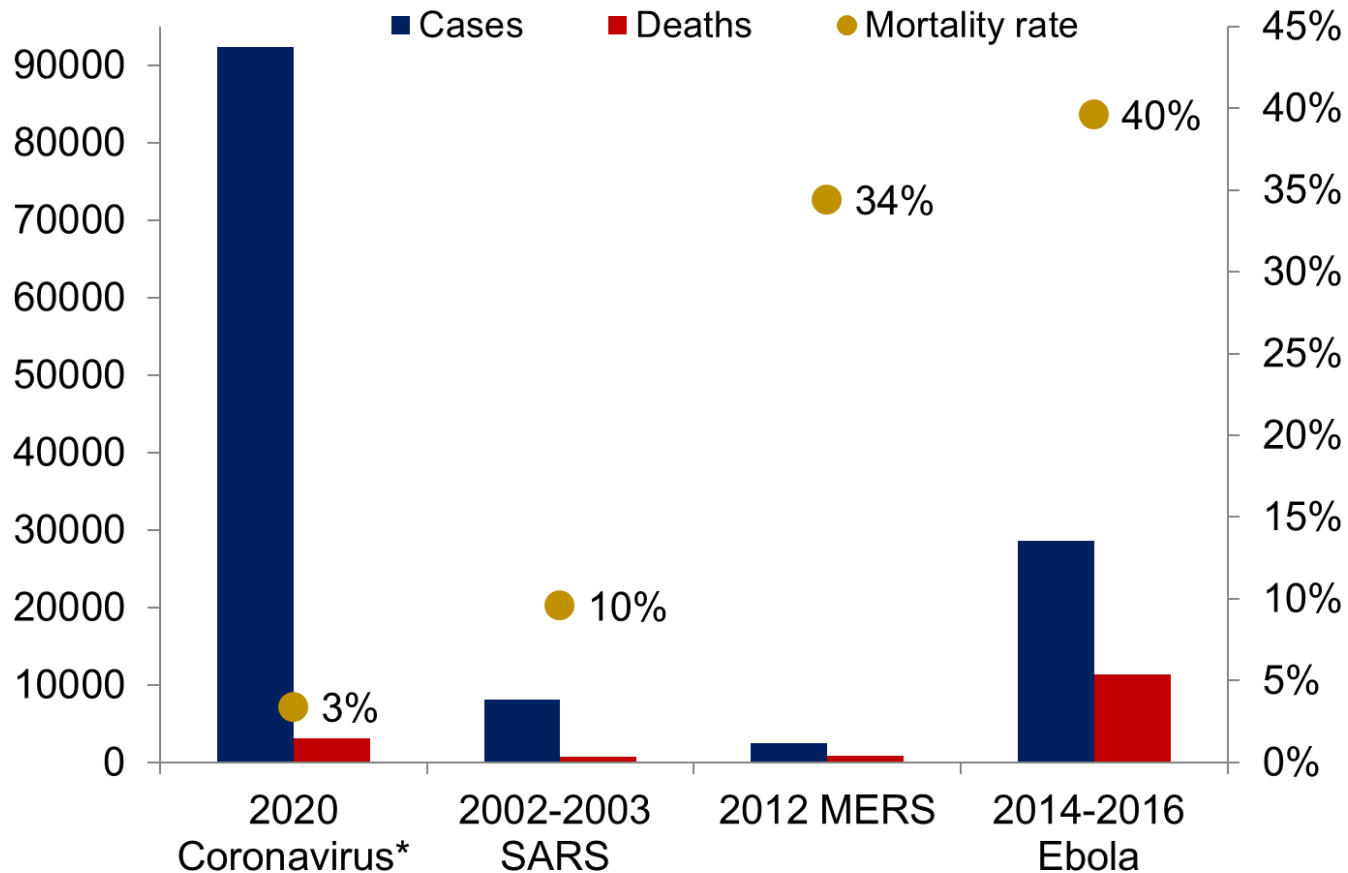
World: PMIs



Source : Oxford Economics/Markit

The coronavirus hit...

Faster spreading virus, but lower mortality rate



Source : Oxford Economics/WHO/CDC

*As of March 3rd, 2020

The coronavirus hit...

Impact of Coronavirus

Travel & Tourism

- Official bans and restrictions
- Reduced appetite for business travel
- Reduce demand for leisure travel

Confidence

- Consumers pull demand forward
- Businesses reduce activity
- Events cancelled
- Lockdown risk

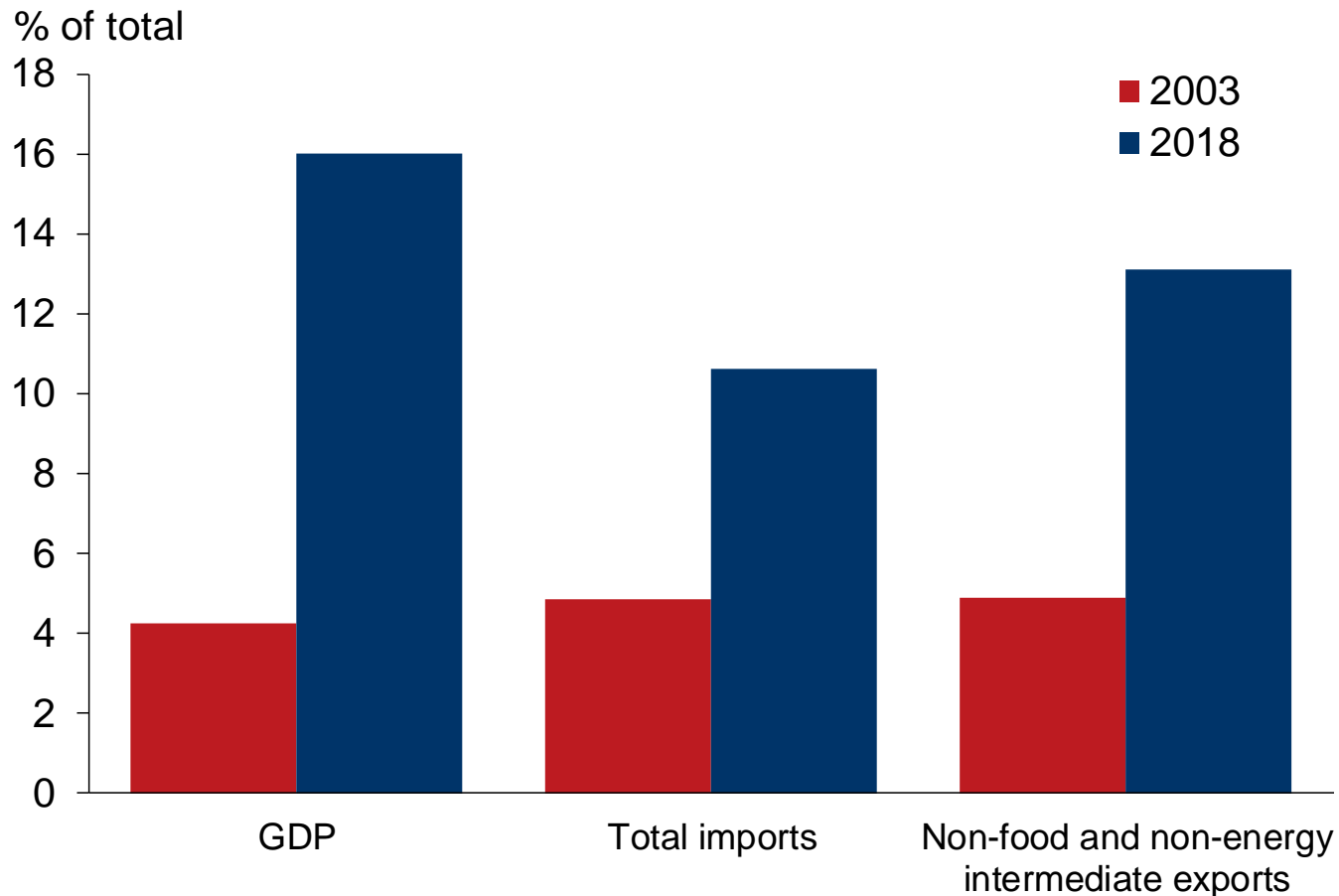
Supply chains

- Inventories run down
- Factory closures in the US
- Lockdown risk

Financial conditions = Accelerator

This time is different because of China's global role

China's importance to the world economy



Source : Oxford Economics/Haver Analytics

And because of the lockdown paradox

Coronavirus: Wuhan U-turn on easing lockdown, as China reports 150 new deaths

Coronavirus: Italy towns in lockdown after COVID-19 deaths

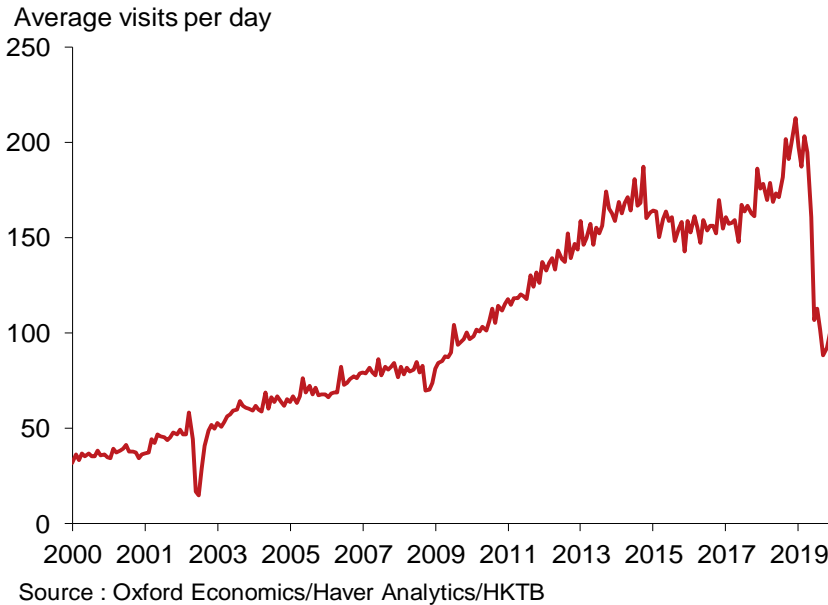
In Coronavirus Crisis, Korean City Tries Openness, a Contrast to China

Coronavirus news: Tenerife hotel in lockdown as tourists tested – live updates

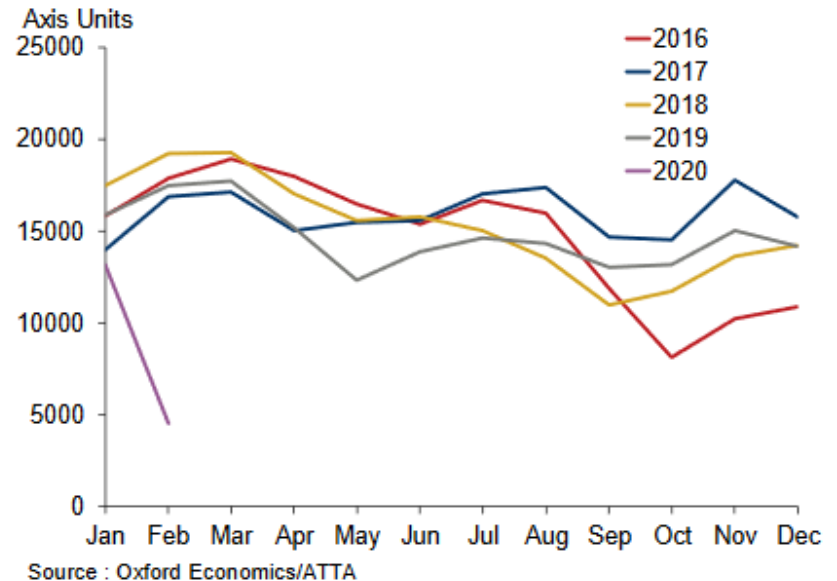
Japan shut down an entire island's schools, restaurants, and stadiums after an uptick in coronavirus cases. Here's what it looks like.

Initial data point to large effects on travel and tourism

Hong Kong: Visitor arrivals



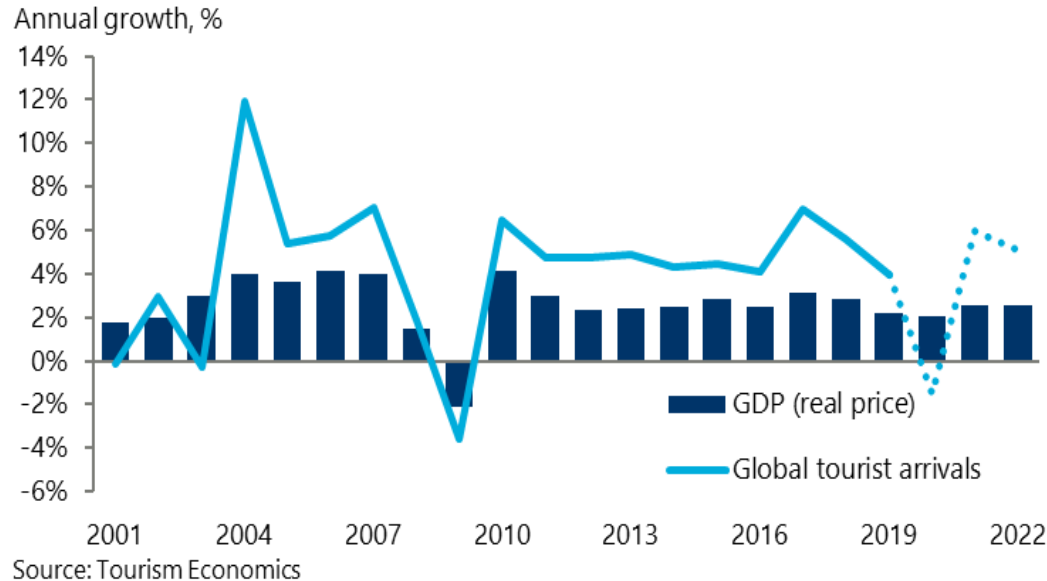
Thailand: International arrivals via air



Thailand daily flight arrivals in the first 20 days of February are 70% lower than the average in February 2019

Global and US travel disruptions will be large

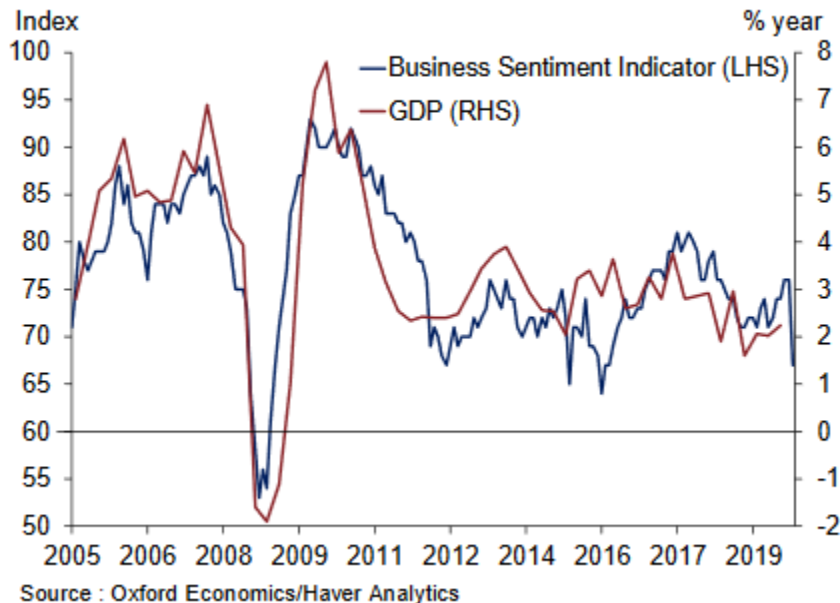
Global GDP & Tourist Arrivals



- Global travel demand is faced with a difficult year ahead, as the outbreak of the coronavirus is set to devastate travel and tourism internationally.
- International arrivals are forecast to decline 1.5-2.0% in 2020, well below global GDP (2.0%) for the first time since the global financial crisis.
- Travel to the US forecast to decline 0.7% in 2020
- Based on historical precedent, a 25% drop in visits to the US from China is expected in 2020 – upward of 1 million visitors each spending \$6,500/trip.

A global confidence shock

South Korea: GDP & business sentiment



Not only did Korea's Business Sentiment Index record a plunge in February, the survey was conducted before outbreak spike

US: Consumer sentiment



No impact in February , but coronavirus mentioned by 20% of those surveyed in last 2 days of the month

PMI readings illustrate forthcoming supply chain disruptions

US ISM PMI® at 50.1%

WHAT RESPONDENTS ARE SAYING

"There are always supply chain challenges with Lunar New Year shutdowns, and this year is no different. **Coronavirus is wreaking havoc on the electronics industry.** Companies are delayed in starting up production, which is resulting in longer lead times, constraints and increased pricing. It's a mad dash to dual source stateside in case China isn't back online soon."
(Computer & Electronic Products)

"January started out strong, but the effects of the **virus in China [and] the continued grounding of the 737 Max** have suppressed new orders. We are still expected to be flat to slightly up [year-over-year] for 2020 sales, based on those issues." (Chemical Products)

"**Layoffs are here.**" (Transportation Equipment)

"**Coronavirus and its impact on the supply chain:** We will see some softness in demand, but also [experience] havoc on items sourced from China that may cause significant delays to production." (Food, Beverage & Tobacco Products)

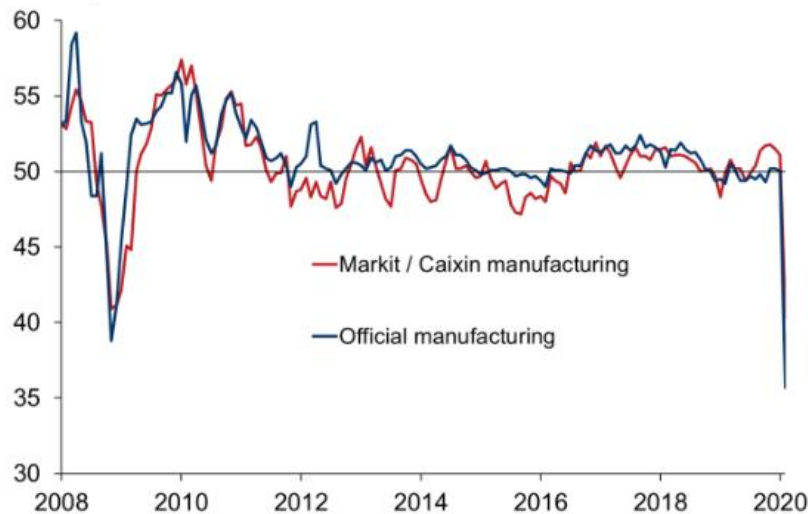
"Energy markets seem to be responding to a potential **drop in demand that may be related to responses [to] the coronavirus.**" (Petroleum & Coal Products)

"**Coronavirus continues to be front** and center as a major supply chain risk to our company. Access to information in China — from our supply base and customers — is slow to come by." (Fabricated Metal Products)

"Sales continue to be strong, with the supply base able to support as required. The major **concern is the China virus** and what that crisis could affect in getting parts. The company is putting plans in place to source out locations, especially in the U.S., for parts." (Machinery)

China: PMIs

Index, 50=Neutral

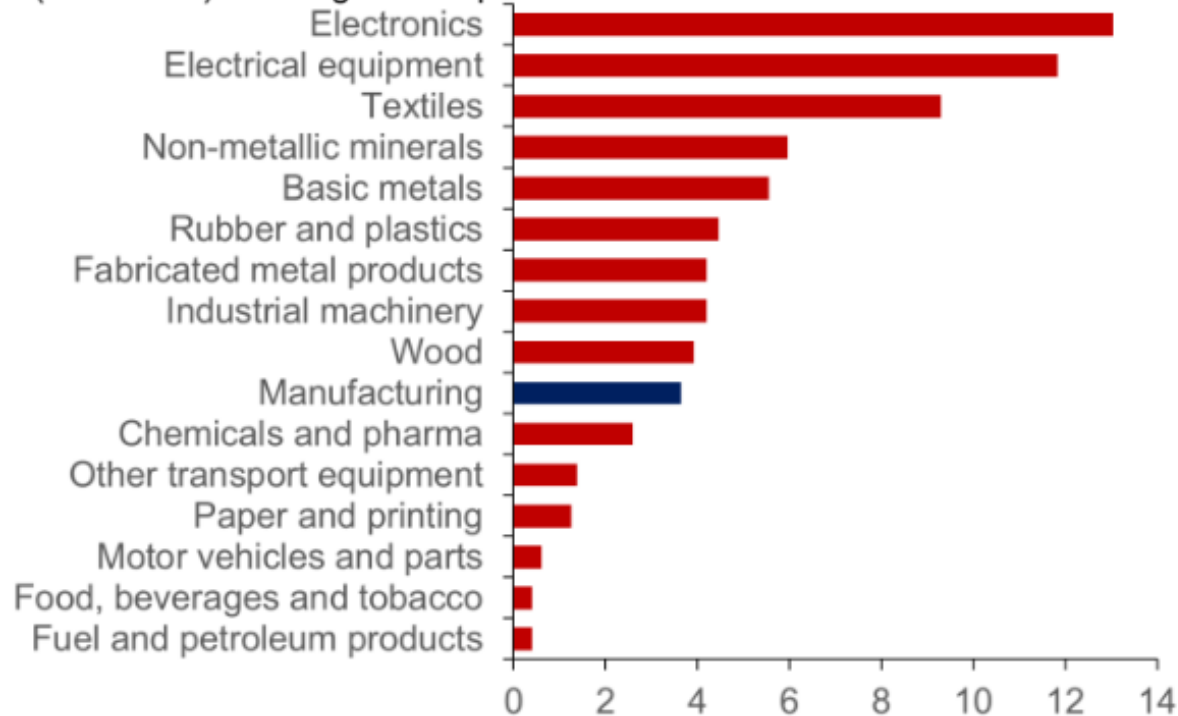


Source: Oxford Economics, CEIC Data, Markit, Caixin

And supply chain disruptions will be significant

Global industrial supply chain vulnerability

Gross exports of intermediate products from China as a share of global (exc China) sector gross output



Source : Oxford Economics/OECD Trade in value-added database

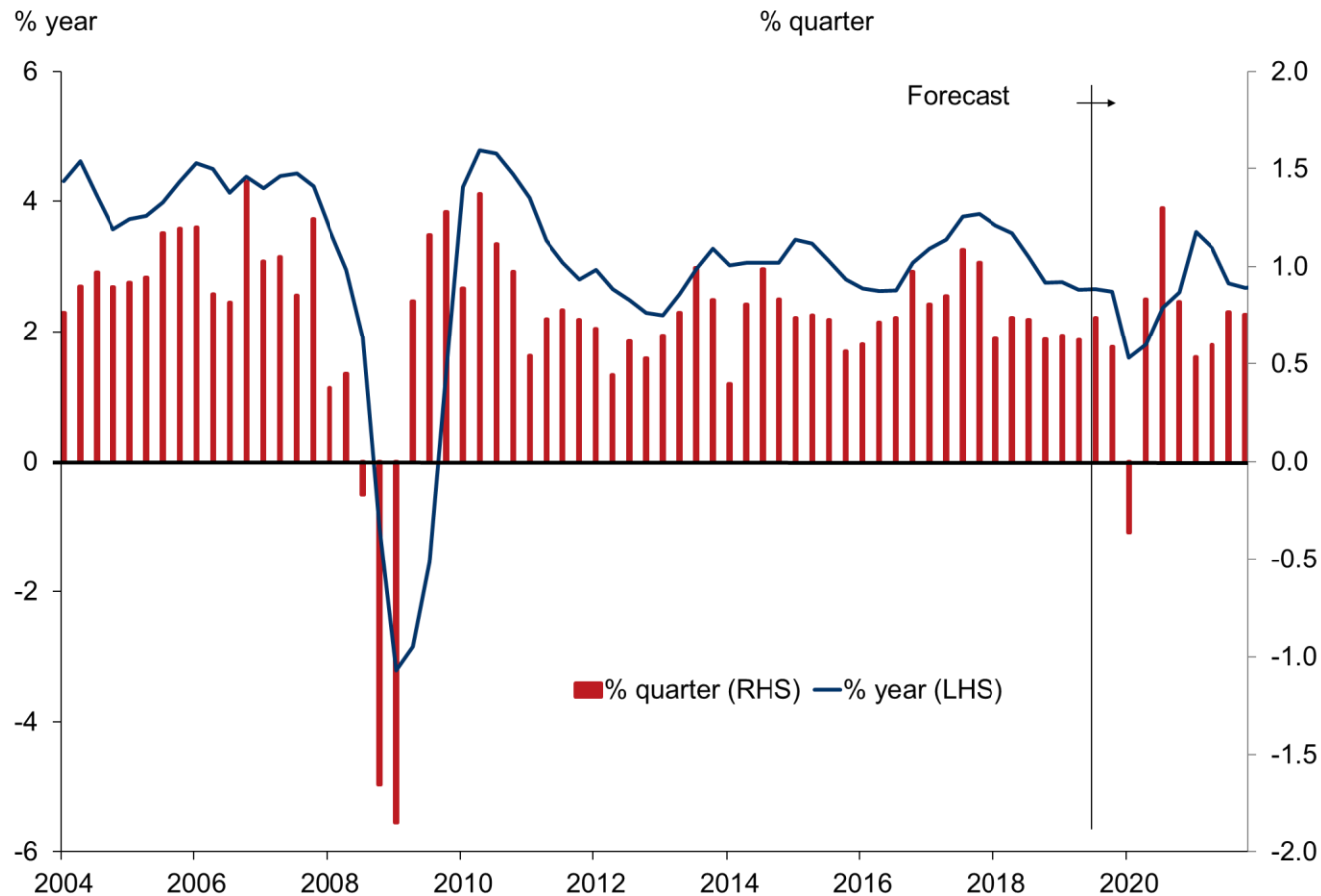
No V-shape recovery -- Slow resumption of activity

China: Coal consumption of 6 power producers



First quarterly fall in world GDP since GFC possible

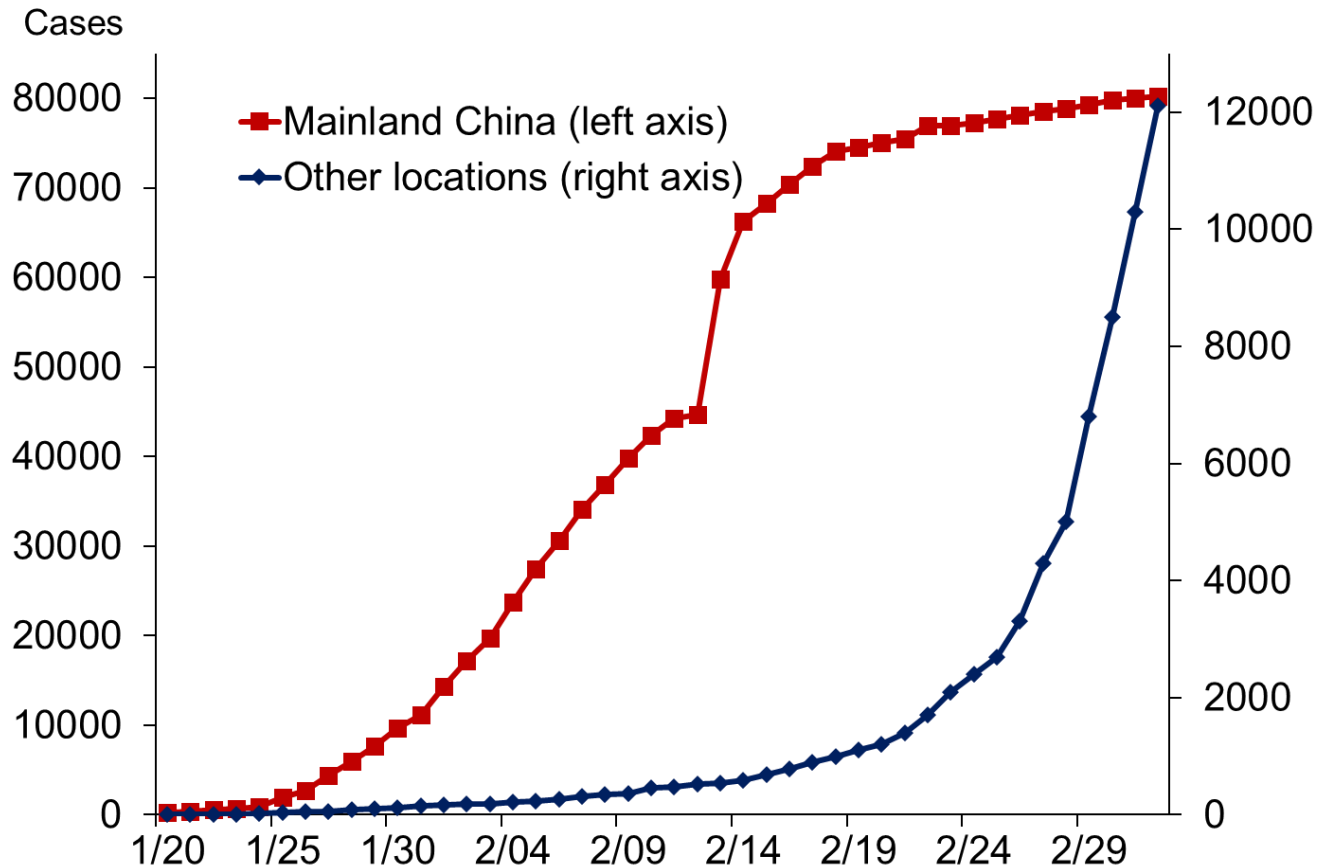
World: GDP



Source : Oxford Economics/Haver Analytics

Exponential rise in global cases lead to renewed fears

Spread of Covid-19 across the globe

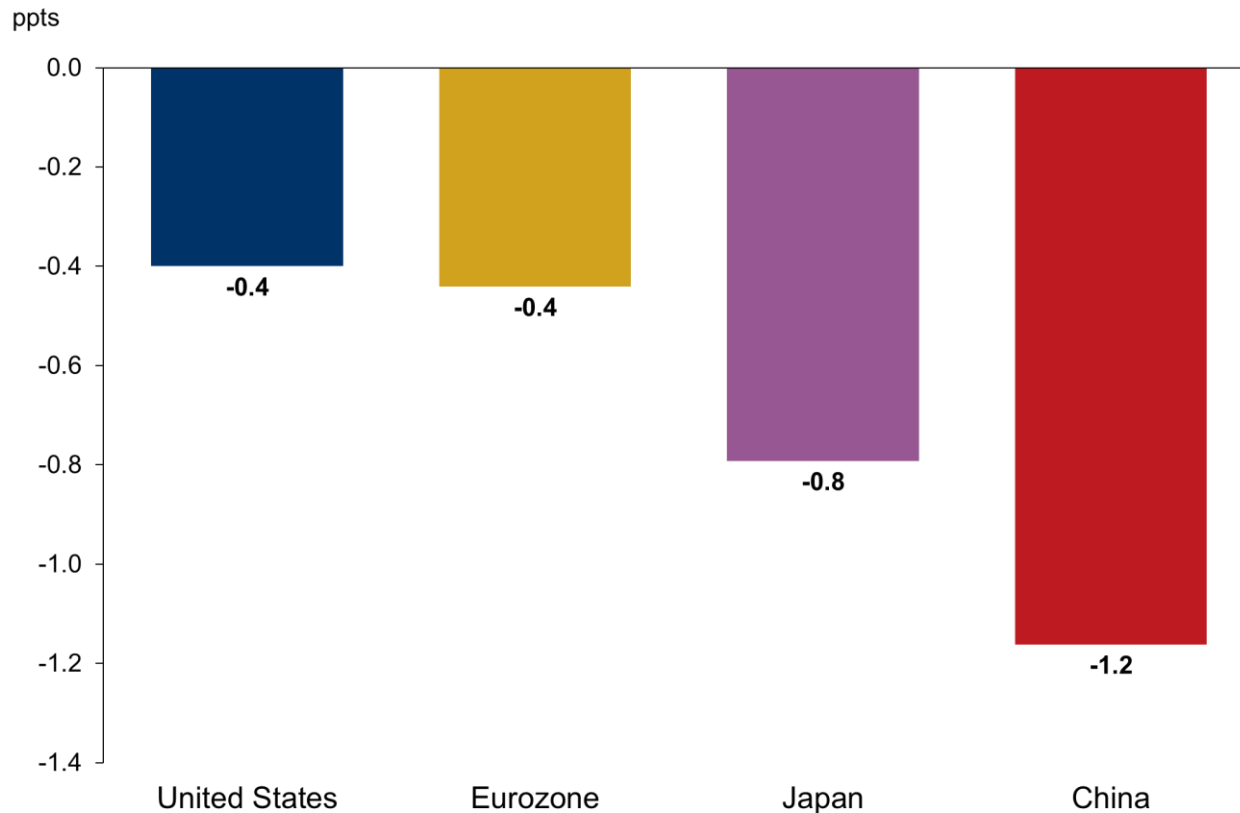


Source : Oxford Economics/PRC NHC

*As of March 3rd, 2020

Asia worst affected but economic damage is spreading

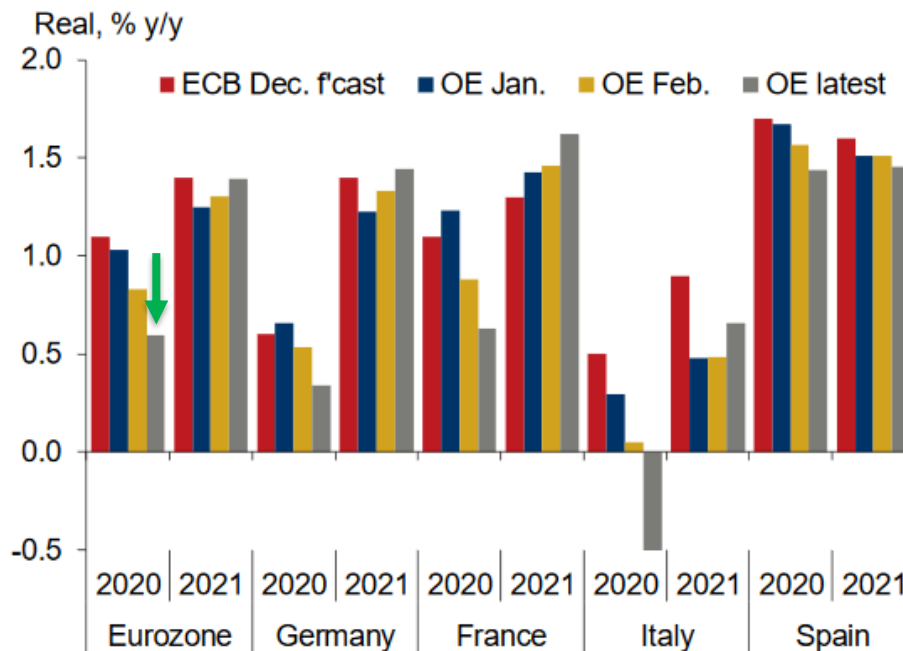
Global: Coronavirus shock to 2020 GDP growth



Source : Oxford Economics

Europe is entering the eye of the storm

Eurozone: OE GDP forecasts vs. ECB

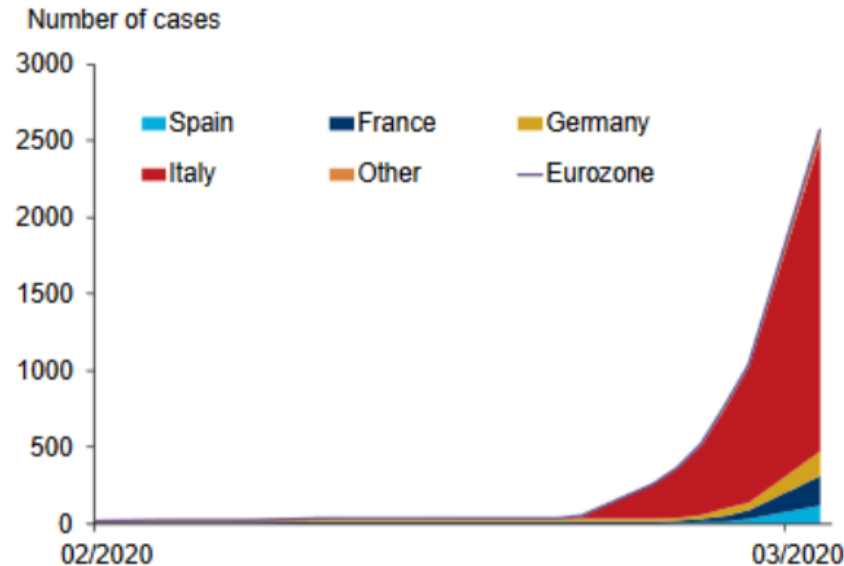


Source: Oxford Economics/Haver Analytics

- We're cutting our 2020 eurozone GDP growth forecast to a seven-year low of only 0.6% from 1.0%.
- Given the extent of the slowdown, elevated risks of a recession in H1 2020, and the region's pre-existing economic fragility, this calls for a timely response from fiscal and monetary policymakers

Various measures considered to alleviate pain

Eurozone: Confirmed coronavirus cases



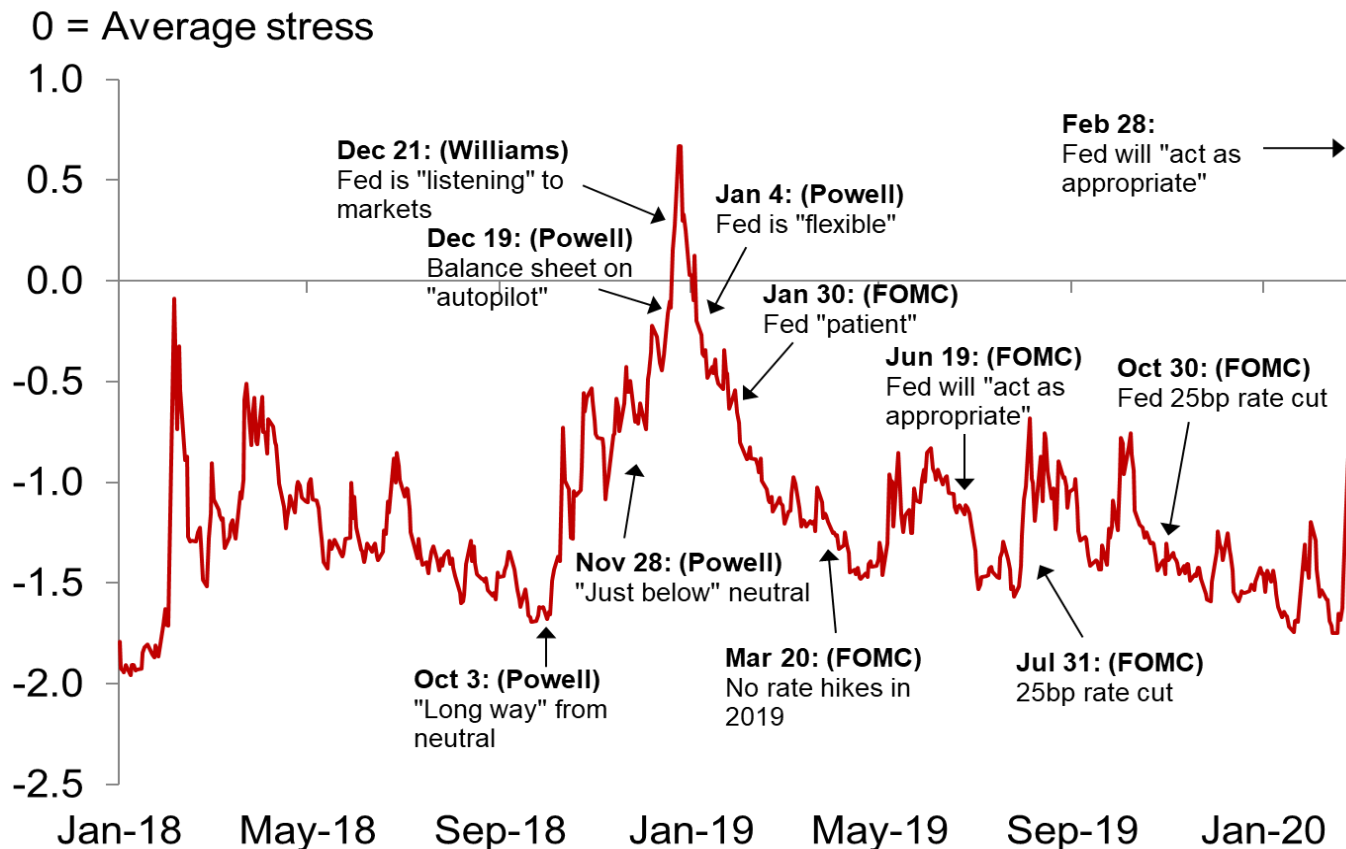
Italy: €3.6bn package (0.2% of GDP), offering tax credits to firms facing a revenue shortfall of 25% or more

Germany: Temporary government-backed credit lines, and “Kurzarbeitergeld” which allows unemployment insurance to cover part of firms’ wage bill to avert layoffs

France: quarantined people may ask the health insurance system to make temporary compensation payments, guarantee loans if they face temporary liquidity issues

Tightening financial conditions amplify the shock

US: Oxford Economics' Financial Conditions Index

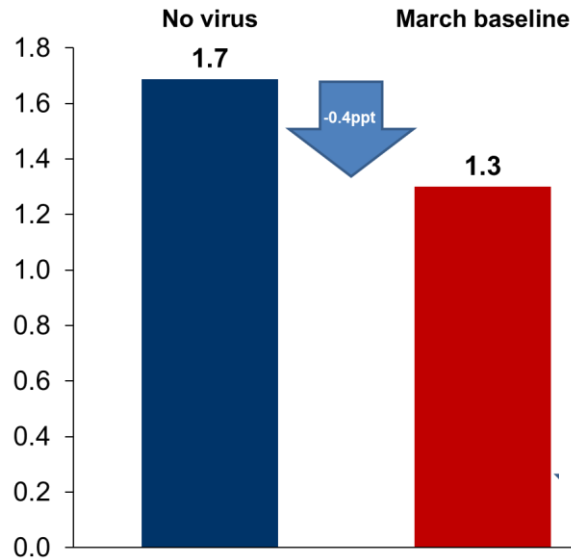


Source: Oxford Economics

The outlook is looking increasingly binary

US GDP growth in 2020

% average

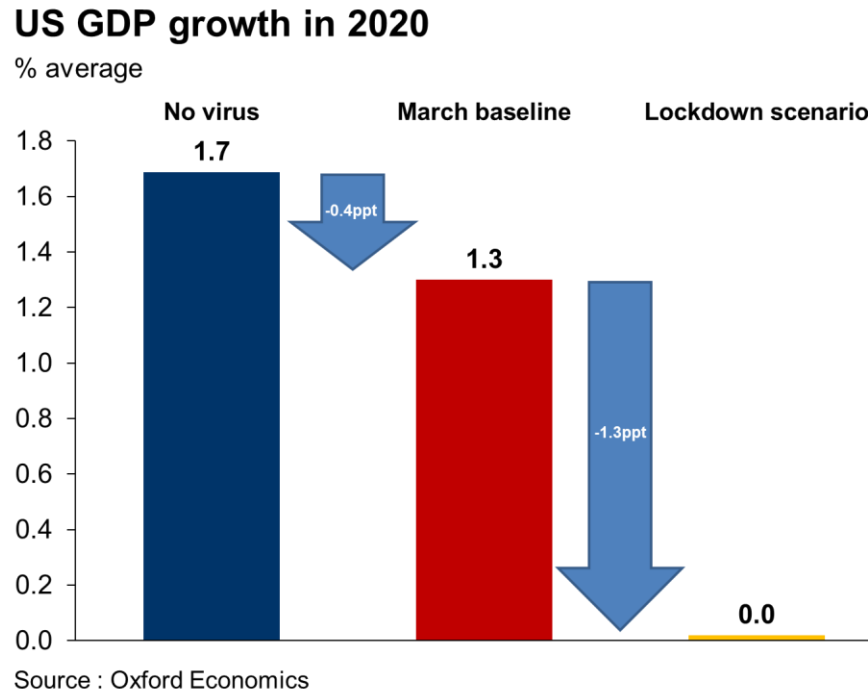


Source : Oxford Economics

Damage on economic output is becoming increasingly visible.

- Official **travel** restrictions and anecdotal evidence of reduced appetite for business travel and curtailed demand for leisure trips point to a direct hit to the sector
- The “**virus fear**” has generated a private confidence shock with anecdotal evidence of a pullback in discretionary spending, precautionary demand for staples, businesses investigating contingency plans and large events being cancelled.
- **Supply chain disruptions** from China to the US

And the lockdown paradox looks like real risk



- We continue to stress the **main economic risk** from the virus is not contagion, or mortality, but rather it stems from the actions that national and local authorities have taken to curb the outbreak – the **lockdown paradox**.
- While our baseline doesn't feature a lockdown scenario, we note that if authorities decide to close schools, severely restrict travel and limit all nonessential movement, the US economy will fall into a recession – with zero GDP growth in 2020 – putting an **end to the longest economic expansion ever**.

What a severe global pandemic would look like

Chart A: World growth falls to an annual rate of just 0.3% in Q2 2020

World: GDP

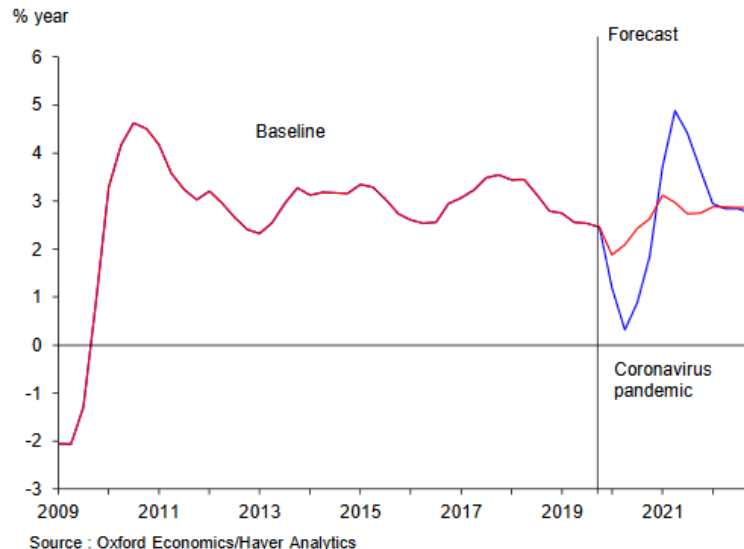
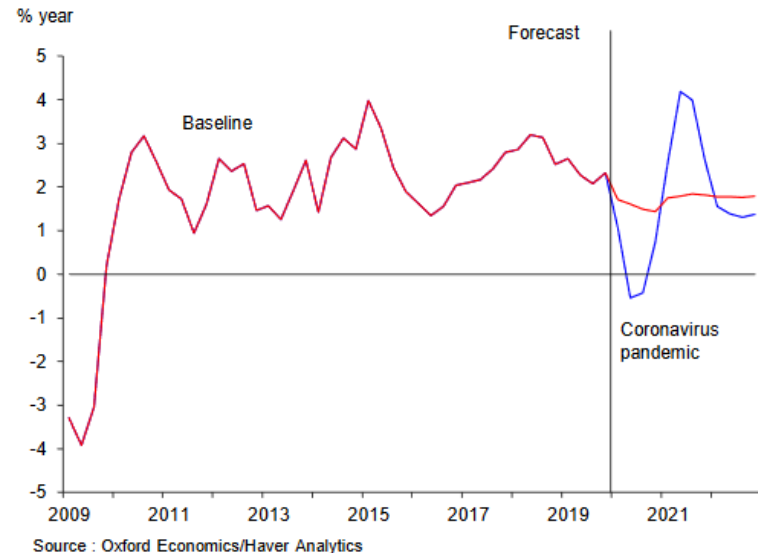


Chart C: US GDP contracts as the global pandemic takes hold

US: GDP



If the coronavirus outbreak becomes a global pandemic, the consequences would be much more severe.

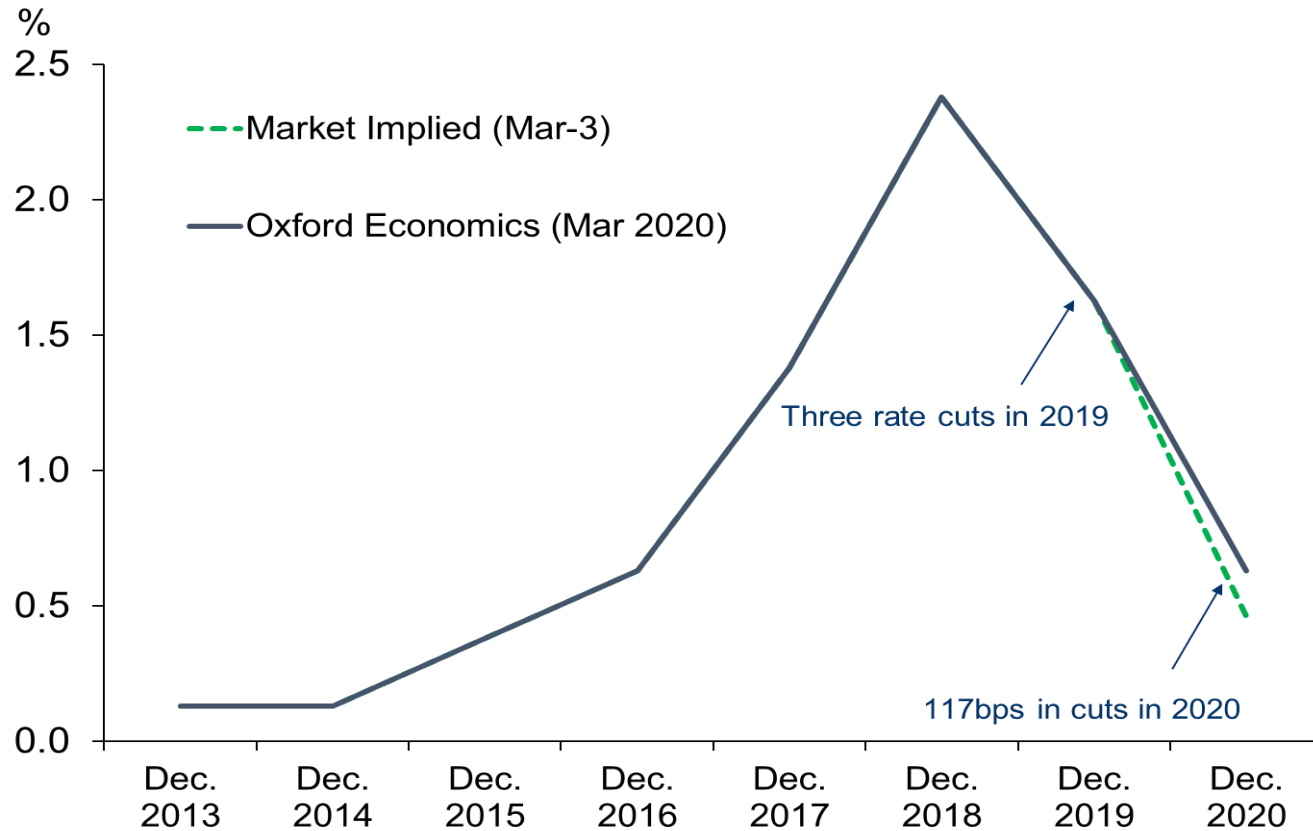
- The virus would put an end to the longest economic expansion on record with GDP tumbling 1.7ppts relative to a no-virus scenario (output loss would surpass \$300bn)
- Overall, global growth falls to an annual rate of just 0.3% in Q2 2020. In 2020 as a whole, growth is just 1.1%, 1.2ppts below baseline, costing over \$1 trillion in lost output

Can the Fed save the day?

Questions: Use the question panel on the right

More rate cuts coming - at least 50bps more

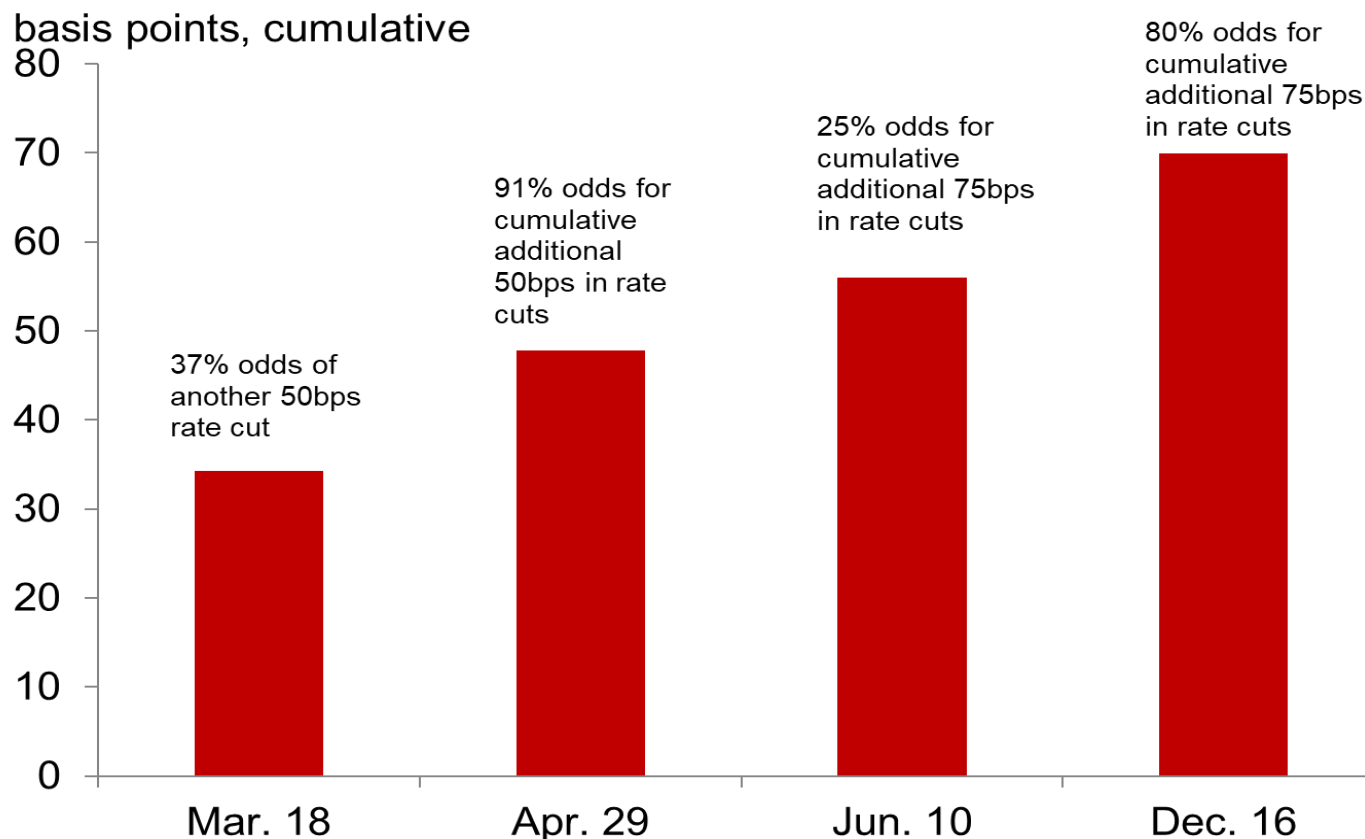
US: Federal funds rate expectations



Source: CME/Federal Reserve/Oxford Economics

Meeting-by-meeting rate expectations

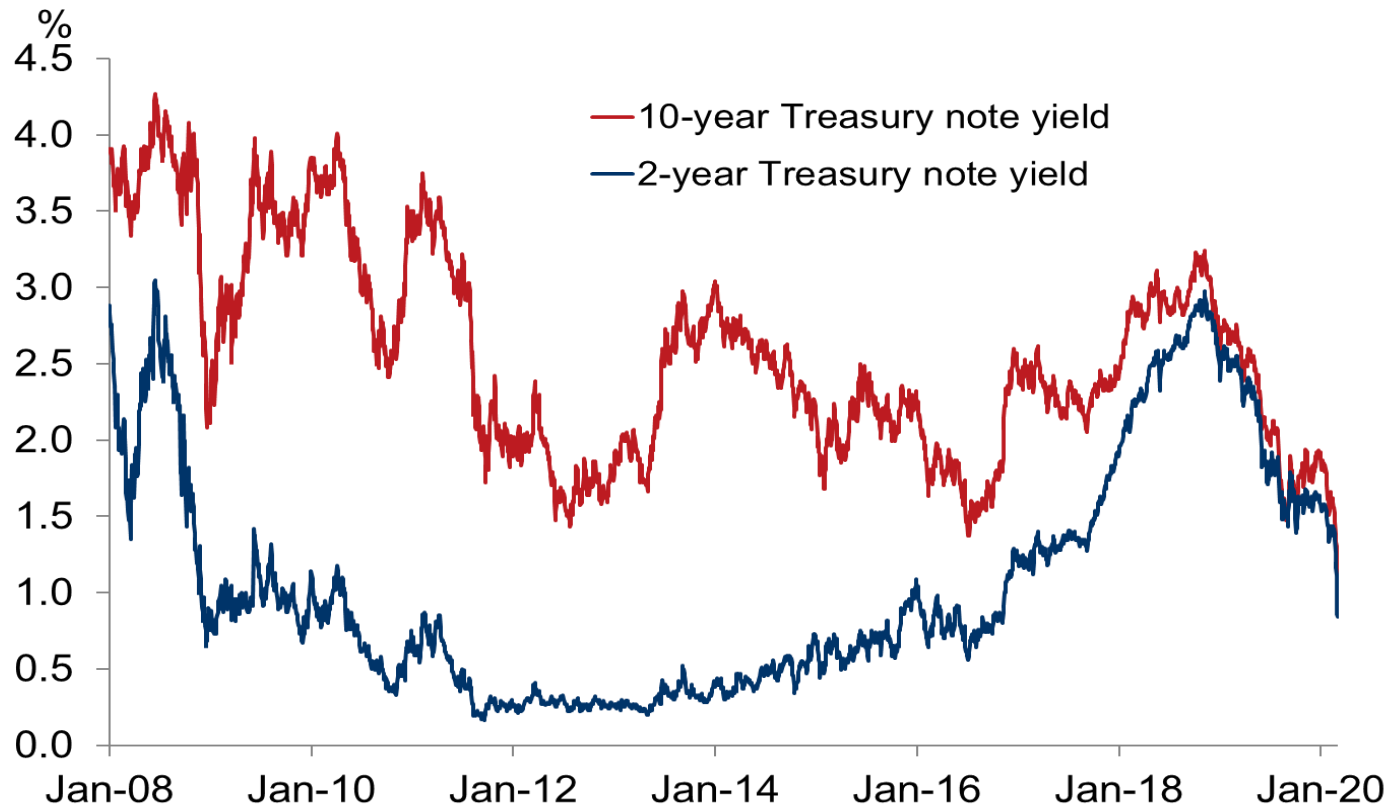
US: Market expectations for further rate cuts



Source : Oxford Economics/Bloomberg

Yields collapsing – 10yr yield fell below 1% for first time

US: Yields collapse across the yield curve



Source : Oxford Economics/Haver Analytics

Coronavirus shock is disinflationary

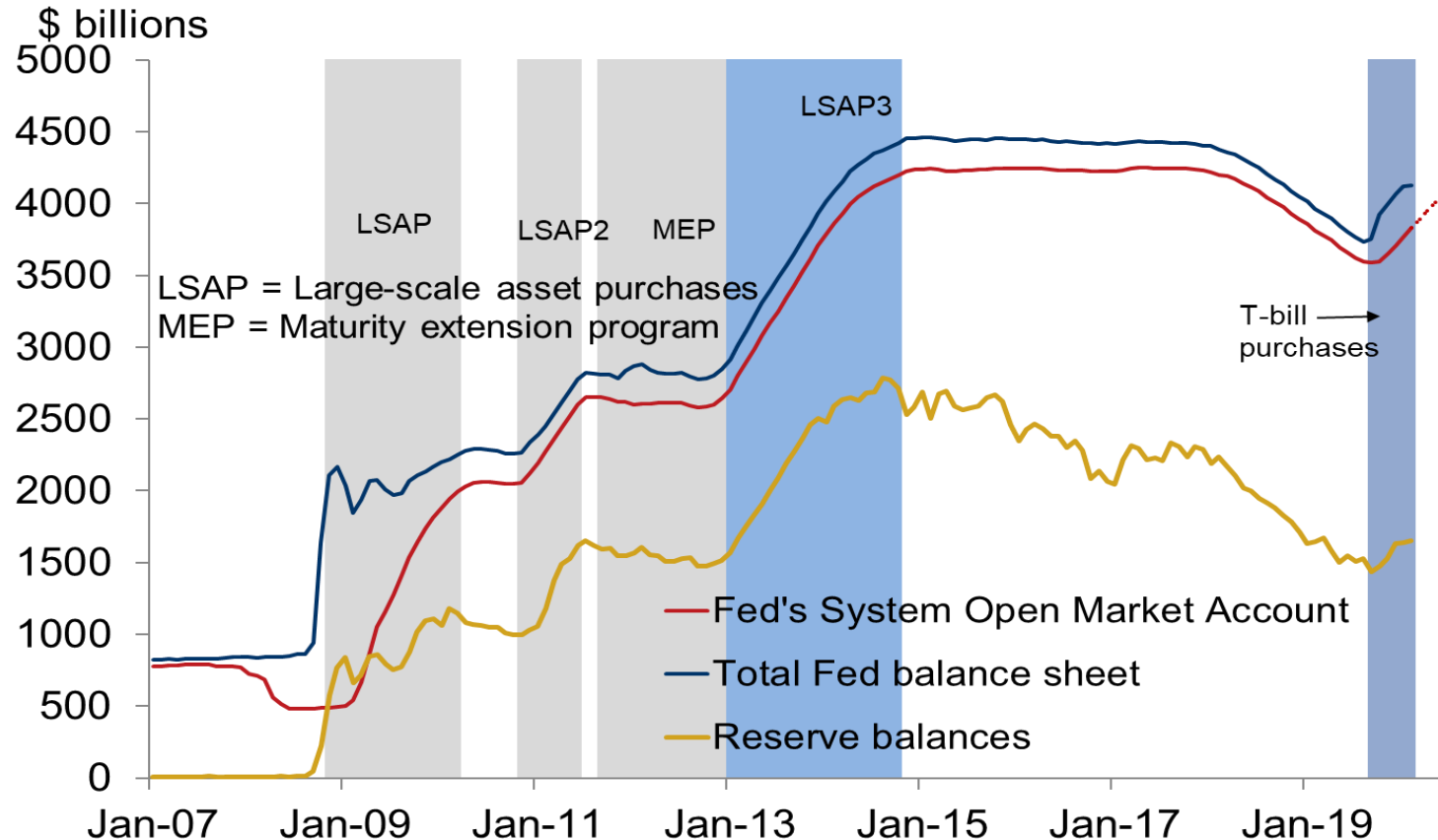
US: Market inflation expectations drop sharply



Source : Oxford Economics/Haver Analytics

Fed to continue to expand the balance sheet and conduct large repo operations

US: Fed balance sheet and bank reserves



Source : Oxford Economics/Haver Analytics

Conclusion

Questions: Use the question panel on the right

Main thoughts

- Coronavirus shock used to represent a supply shock for China and rest of world, but it's rapidly transformed into demand shock too
- Demand-side disruptions are visible in travel activity, confidence shock, fear factor affecting consumers and businesses
- Supply chain disruptions initially represented indirect shock to RoW, but increasingly we're observing direct shock across world
- Lockdown paradox is most import risk
- Financial condition are acting as an amplifier
- Fed easing won't stop the virus, or help supply chains, but it can support confidence, ease financial conditions and lower cost of capital
- Coordinate G-7 action is needed but emphasis should be on health, social and credit/liquidity measures

We are looking to support you during these uncertain times with **3-month access** to:

- ***All of our Research Briefings***

Receive all the latest research updates from Oxford Economics to monitor the global and regional impact of the coronavirus, the implications for financial markets as well as all of our current thematic research on global economic developments.

- ***Our Global Scenario Service***

This service allows you to quantify the effects of the coronavirus spread on our baseline forecasts for the 80 most important countries and compare this with our latest coronavirus pandemic scenario as well as to other current global risk scenarios, such as US or world recession.

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THANK YOU!

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