BESA PERSPECTIVES
THE BEGIN-SADAT CENTER FOR STRATEGIC STUDIES

The Effect of Coronavirus on the Global Economy

by Dr. Frank Musmar

BESA Center Perspectives Paper No. 1,495, March 20, 2020

EXECUTIVE SUMMARY: The 2020 outbreak of the novel coronavirus (COVID-19) will go down in history for its massive impact on the global economy and on public health, both physical and psychological. At some point, life will get back to normal, but it will not be the same as it was before. People have been panic buying over the past two weeks as they wake up to how unprepared they are for a crisis. As a result, many are rethinking their spending habits and what necessities they should have on hand. Some of these temporary adaptations will become permanent as people discover that they prefer them to old ways of doing business.

China is being severely affected by the outbreak of the devastating coronavirus (COVID-19). The Chinese manufacturing and services sectors plunged to record lows in February, Chinese automobile sales sank a record 80%, and Chinese exports fell 17.2% in January and February. Official data confirm a widespread slowdown in China's economic activity, a trend that is also visible through informal barometers like low pollution levels and depressed shipping traffic. The country's economic recovery will be difficult as demand from other countries continues to drop while they attempt to cope with the spread of the virus within their own borders.

Among the other major global economies, the OECD forecasts the most significant downward growth revisions in countries deeply interconnected to China, especially South Korea, Australia, and Japan. Europe and Japan are likely already in recession territory, given their weak fourth-quarter performance and high reliance on trade. While the US entered the crisis with a tailwind, some analysts are forecasting a contraction in US GDP in the second quarter.

As the global supply chain slows down, the world is starting to pay closer attention to its reliance on China, and anyone conducting business with that country is feeling the pinch. As a result, a trend that will most likely follow the coronavirus outbreak will be a move away from reliance on China and toward greater self-sufficiency on both an industrial and a personal level. Industries that have been relying heavily on China, such as manufacturing, will likely reconsider their business ties and move parts of their operations elsewhere to diversify risk.

A range of banks and financial institutions have offered worst-case scenarios for 2020 as the spread of the virus affects the global economy and roils financial markets. The extent of the damage will depend on how quickly the virus is contained, the steps authorities take to contain it, and how much economic support governments are willing to provide to stem the epidemic's impact and immediate aftermath. Bitcoin (BTC) has moved largely in line with the stock market and slid back below the $10,000 mark as coronavirus fears hit the global markets. Overall, however, bitcoin market sentiment remains positive in light of the upcoming block reward halving and the expected rally that has historically always followed halving.

Global markets are the first to react to a crisis. When it became clear that the coronavirus was not going away anytime soon, stock markets across the globe took a hit. After the CDC issued a public warning about the coronavirus, the S&P 500 Index had its worst week since the 2008 global financial crisis, dropping by over 11% in the last week of February. Conversely, the yield of the benchmark 10-Year US Treasury hit an all-time low as investors moved out of risky assets and into safe-haven assets. Gold also experienced a spike, adding to its strong rally since the start of the year. The price of oil has skidded 18% since the beginning of the outbreak. When the global supply chain expects a usage slowdown, oil is usually the first to drop in value as demand declines.

Tourism and travel-related industries will be among the hardest hit as authorities encourage "social distancing" and consumers stay indoors. The International Air Transport Association warns that coronavirus could cost global air carriers between $63 billion and $113 billion in revenue in 2020, and the international film market could lose over $5 billion at the box office. Similarly, shares of major hotel companies have plummeted in the past few weeks, and entertainment giants like Disney expect a significant blow to revenues. Restaurants, sporting events, and other services will also face significant disruption. Industries less reliant on high social interaction, such as agriculture, will be comparatively less vulnerable but will still face challenges as demand wavers.

The foremost positive financial impact of coronavirus will be seen in telecommuting and remote working, and we can expect to see a boom in freelancing, remote job, and remote software applications such as Zoom and Slack. Some corporations have started to offer staff work-from-home options to compete with remotely driven startups. This trend is poised to accelerate in the coming months as companies ask more and more employees to work from home. Teleconferencing is an obvious winner, perhaps too obvious to be capitalized on; Zoom Video Communications is already trading at 1,250 times earnings. A more affordable stock is Dell Technologies, which will benefit when employers upgrade the laptops used by remote workers. Telecommuting will permanently damage US demand for gasoline.

According to Datawrapper, the stock price year to date (%) winners due to coronavirus are Zoom Video Communications with a price/earnings ratio of 1,250, followed by Netflix (89), Amazon (83), Cerner (44), Thermo Fisher Scientific (34), K12 (26), and Quest Diagnostics (18).

Dr. Frank Musmar is a financial and performance management specialist and a non-resident associate at the BESA Center.