

ECONOMIC OUTLOOK

Understanding the Global Coronavirus Recession

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8 Apr 2020

Research Briefing | US
Understanding the coronavirus sudden stop

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The Global Coronavirus Recession (GCR) marks the end of the longest US economic expansion on record, and it will feature the sharpest economic contraction since WW2. The sudden stop in private sector activity will be partially offset by massive public sector spending and unprecedented monetary policy stimulus, but even so, the employment losses will be traumatic, and the rebound post-crisis will be U-shaped with a full recovery taking 12 to 18 months.

Assuming 10-12 weeks of social distancing from mid-March, we anticipate real GDP will drop by over 10% in Q2, with a gradual recovery starting in late March, followed by a very gradual reduction of social distancing measures thereafter.

9 Apr 2020

Country Economic Forecast
United States

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The Global Coronavirus Recession (GCR) not only marks the end of the longest US economic expansion on record, but it will also lead to the sharpest contraction in activity since WW2. The now expected real GDP will contract around 4% in 2020, assuming a 13-week lockdown starting in late March, followed by a very gradual reduction of social distancing measures thereafter.

High-frequency indicators show that spending on restaurants has come to a near full stop, home occupation is only about 20%, retail spending on brick and mortar stores is down over 40%, and road congestion across the nation is about 71% lower than last year. We estimate real GDP will shrink more than 30% annualized in Q2 – nearly 2.5 times larger than the output loss from the GFC.

A decade-long streak of monthly employment gains **ended abruptly in March**, as the initial effects of the coronavirus pandemic led to a sharp job loss of 701,000. But, while the report may have looked dark, it fell in comparison to the expected 24 million job losses in April. We foresee the unemployment rate surging to 14% in April and 16% in May, with a cumulative job loss over two months of around 27 million – three times more than during the GFC.

Unprecedented **tax stimulus** and **unprecedented fiscal support** will provide an essential lifeline to the economy. But, even with \$2.3T of stimulus – including a major increase in business lending capacity – the new normal for the year will feature only a gradual relaxation of social distancing measures and a slow recovery until a medical solution to coronavirus ends the crisis.

Given the severity of the economic and labor market shock and the expectation for a gradual and uneven easing of lockdown measures in Q2, we forecast U-shaped rebound with the productivity **growth rate** being the longest to recover.

Forecast for United States		2018	2019	2020	2021	2022	2023	2024
GDP	1.4	2.1	2.1	-4.0	1.5	2.5	2.5	2.5
Private Consumption	1.0	1.0	-0.7	4.4	1.9	2.0	2.0	2.0
Government Spending	4.1	1.9	0.0	4.2	2.2	2.0	2.0	2.0
Exports of Goods and Services	3.0	0.0	0.0	7.5	3.5	3.5	3.5	3.5
Imports of Goods and Services	4.4	1.0	-0.1	4.1	2.1	2.0	2.0	2.0
Investment in Fixed Capital	1.0	0.0	-0.5	1.7	2.0	2.0	2.0	2.0
Inventory Investment	0.4	0.4	0.1	0.1	0.1	0.1	0.1	0.1
Net Exports of Goods and Services	-1.4	-1.0	-0.1	-0.4	-0.7	-0.5	-0.5	-0.5
Change in Government Debt	1.0	1.0	0.0	0.0	0.0	0.0	0.0	0.0
Change in Net Foreign Assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Change in Net International Investment Position	1.0	1.0	0.0	0.0	0.0	0.0	0.0	0.0
Change in Net International Investment Position (excl. Govt)	1.0	1.0	0.0	0.0	0.0	0.0	0.0	0.0

Source: Oxford Economics
Last Updated: 8 Apr 2020

Global: CPI inflation % year on year

— Current baseline
— Downside scenario
— Pre-coronavirus baseline

Germany: GDP, real, LCU

— Current baseline
— Downside scenario
— Pre-coronavirus baseline

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Q1	1.74	4.82	2.17	0.58	0.84	-0.54	2.34	1.10	2.08	2.03	1.48	1.09	0.83
Q2	1.75	-6.61	4.27	3.86	0.82	0.51	1.58	1.60	2.05	1.87	1.38	1.02	0.83
Q3	0.53	-0.71	4.68	3.28	0.88	0.82	1.17	1.91	2.23	1.78	1.17	1.00	0.95
Q4	1.76	-2.95	4.46	2.43	0.12	1.04	1.46	1.84	2.10	1.83	1.12	0.90	0.96
Total 2020	-20.192	70.799	16.052	2.490	1.827	0.231	6.462	6.604	6.604	7.953	5.103	4.695	3.756
% Change	5.92	-77.94	171.04	-5.31	-33.36	-33.74	298.08	1.75	33.88	-15.18	-29.32	-20.50	-7.40

US OUTLOOK WEBINAR

Global Coronavirus Recession brings US economy to sudden stop

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U.S. TREASURY YIELDS

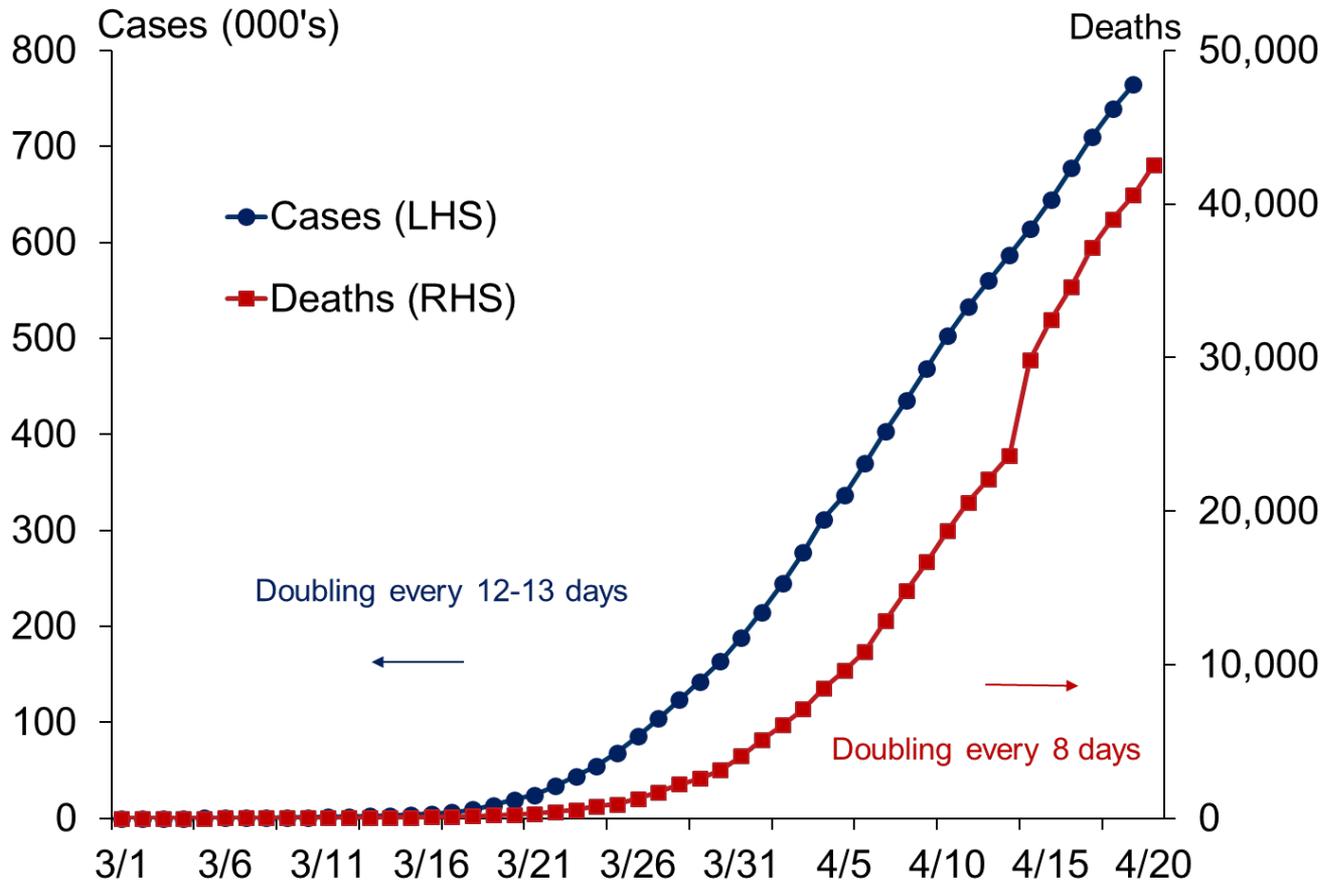
2 Year	0.7011%	-0.1249
5 Year	0.7431%	-0.1209
7 Year	0.8893%	-0.1067
10 Year	0.9990%	-0.0890
30 Year	1.6127%	-0.0323

MARKET SELL-OFF | DACO: FED'S SURPRISE CUT NOT ENOUGH TO LIFT MKT OPTIMISM

CNBC

“Flattening the curve” is extremely difficult

US: The coronavirus outbreak at national level



Source : Oxford Economics/COVID Tracking Project

As of April 21st, 2020

Economics of 'fear' + Economics of 'sudden stops'

Health

- Rapid contagion
- Stress on healthcare system
- Elevated mortality

Demand

- Confidence plunges
- Businesses reduce activity
- Consumer spending falls
- Travel/Tourism stalls
- Unemployment surges

Supply chains

- China disruption
- Inventories run down
- Factory closures in the US

Lockdown paradox

Financial Stress

Oil price shock

Yet it is essential to avoid a complete collapse of system

Flattening the Pandemic curve

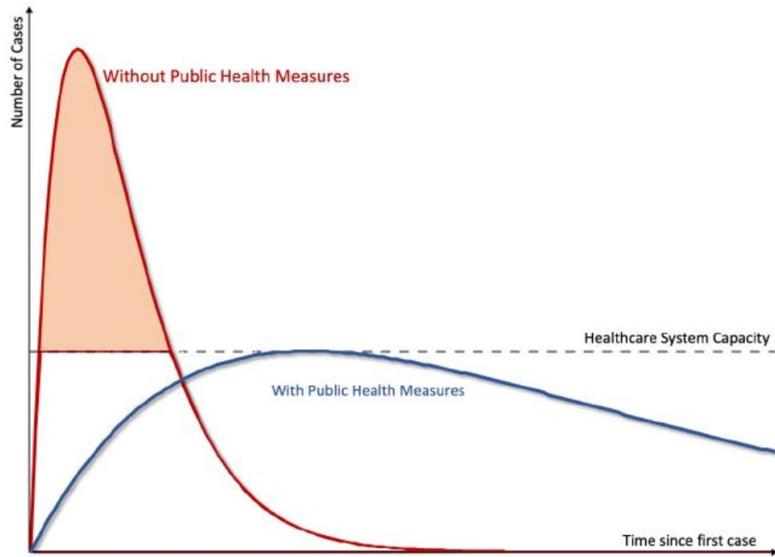


Figure 1: Flattening the Pandemic Curve

Flattening the Recession curve

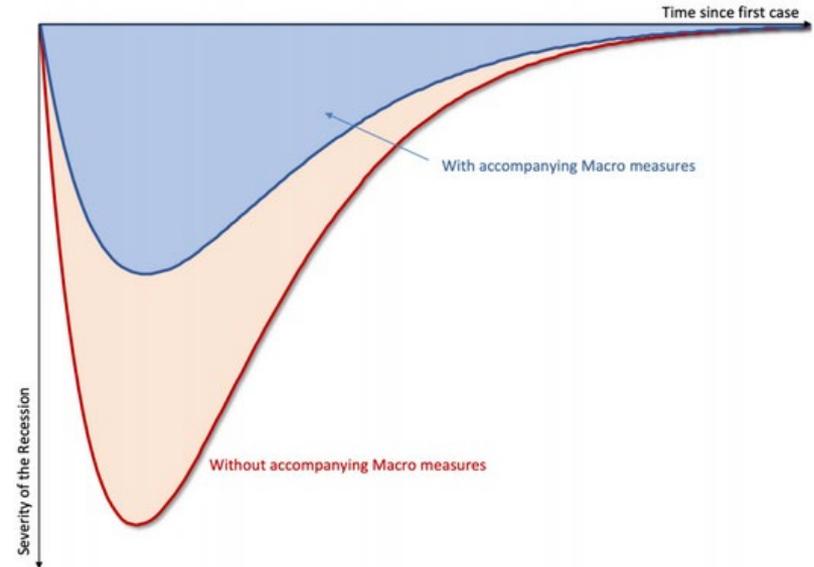
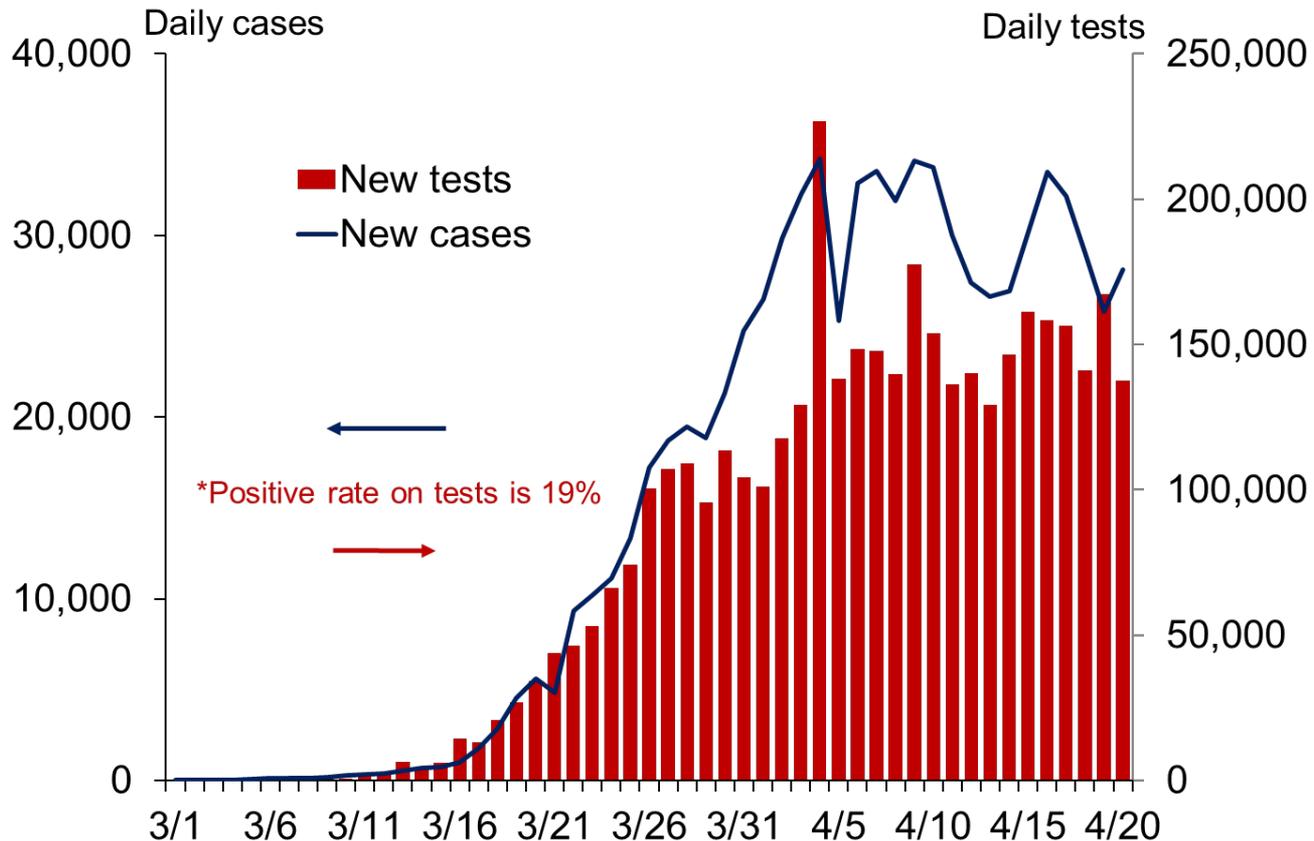


Figure 2: Flattening the Recession Curve

Source: “Flattening the Pandemic and Recession Curves” Pierre-Olivier Gourinchas, UC Berkeley, March 2020

Testing (& tracing) capacity needs to be increased tremendously

New US coronavirus cases & testing*



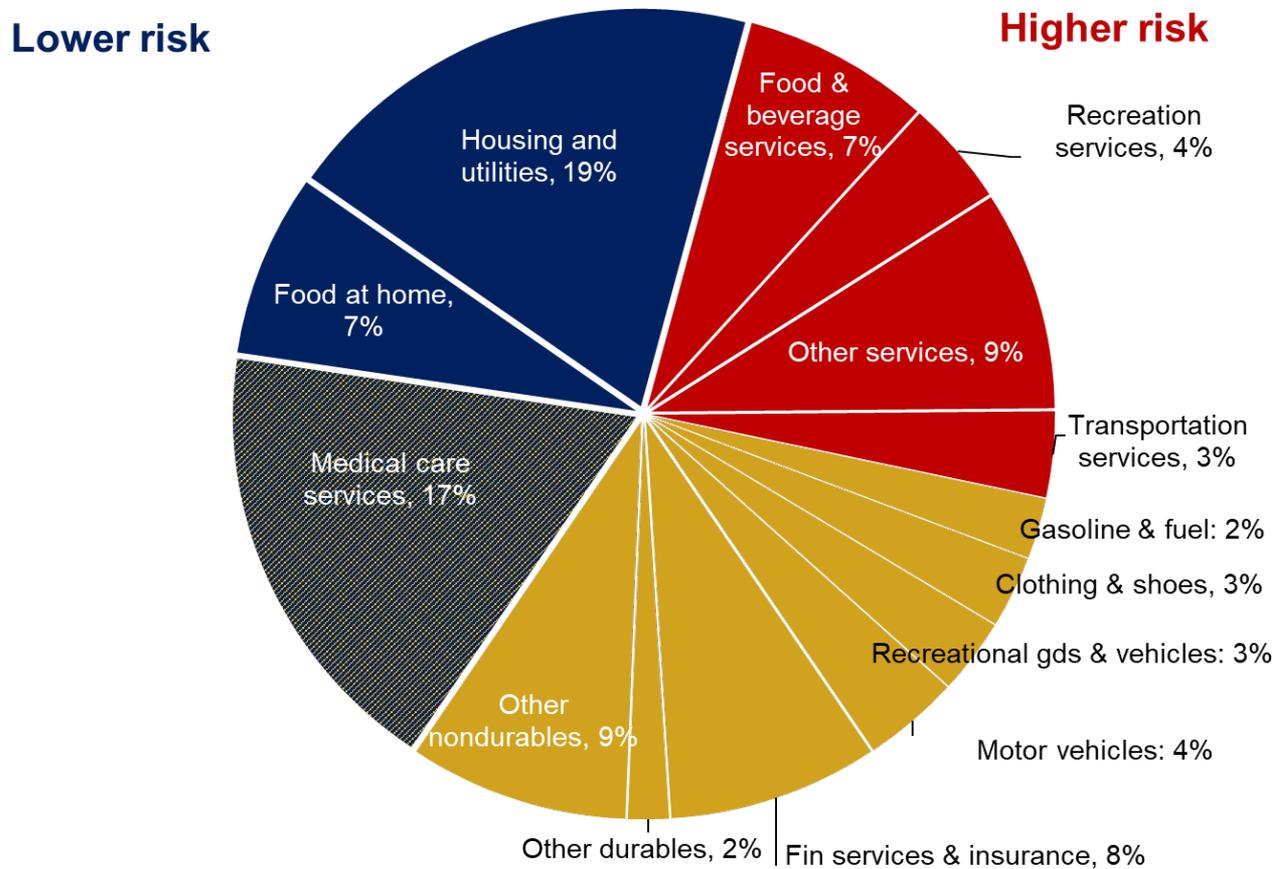
Source : Oxford Economics/COVIDTRACKING

*As of April 20th, 2020

Severe disruptions across sectors

Over 50% of consumer spending is at risk

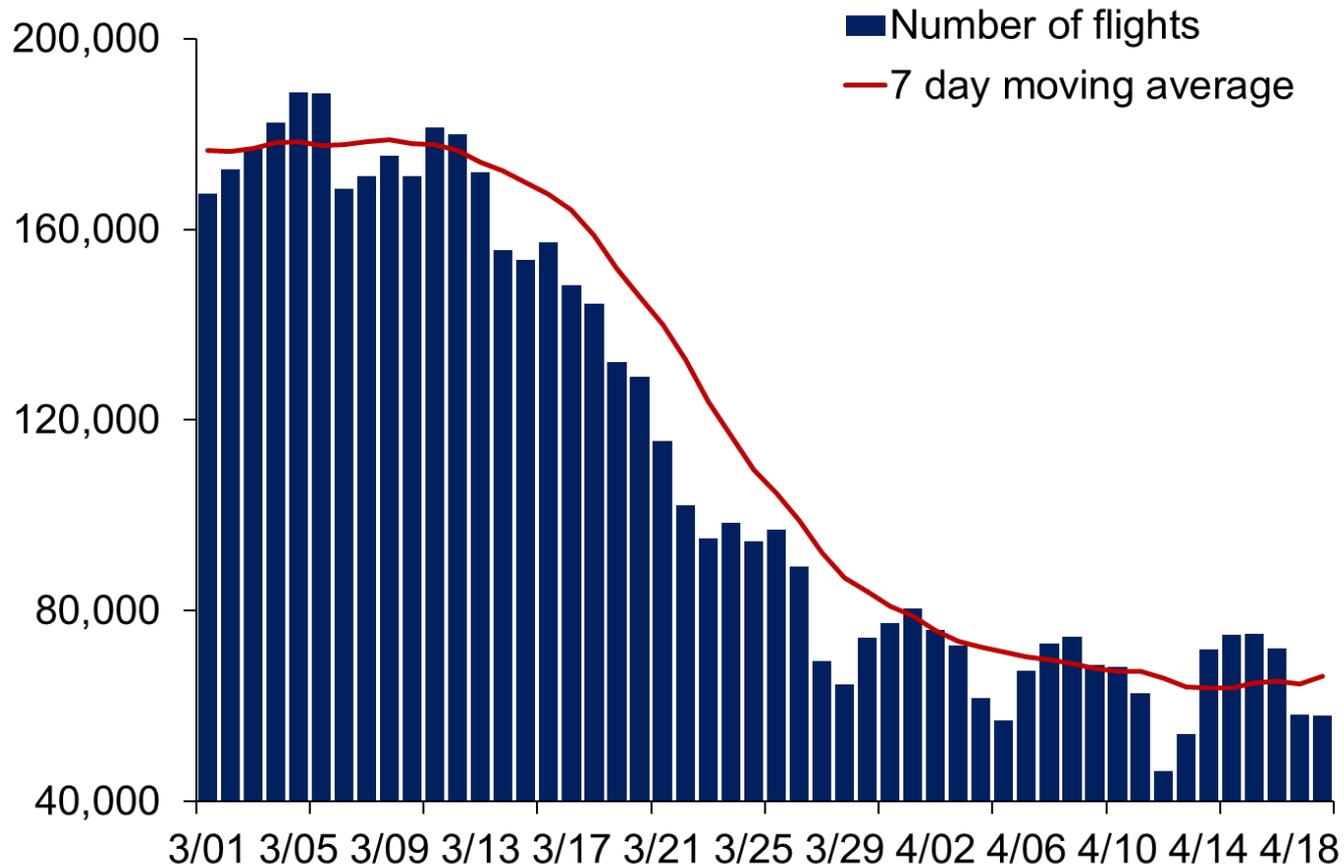
US: Consumer spending at risk from virus



Source : Oxford Economics/Haver Analytics

A 75% decline in air traffic & 95% in TSA throughput

US: Dramatic fall in global air traffic

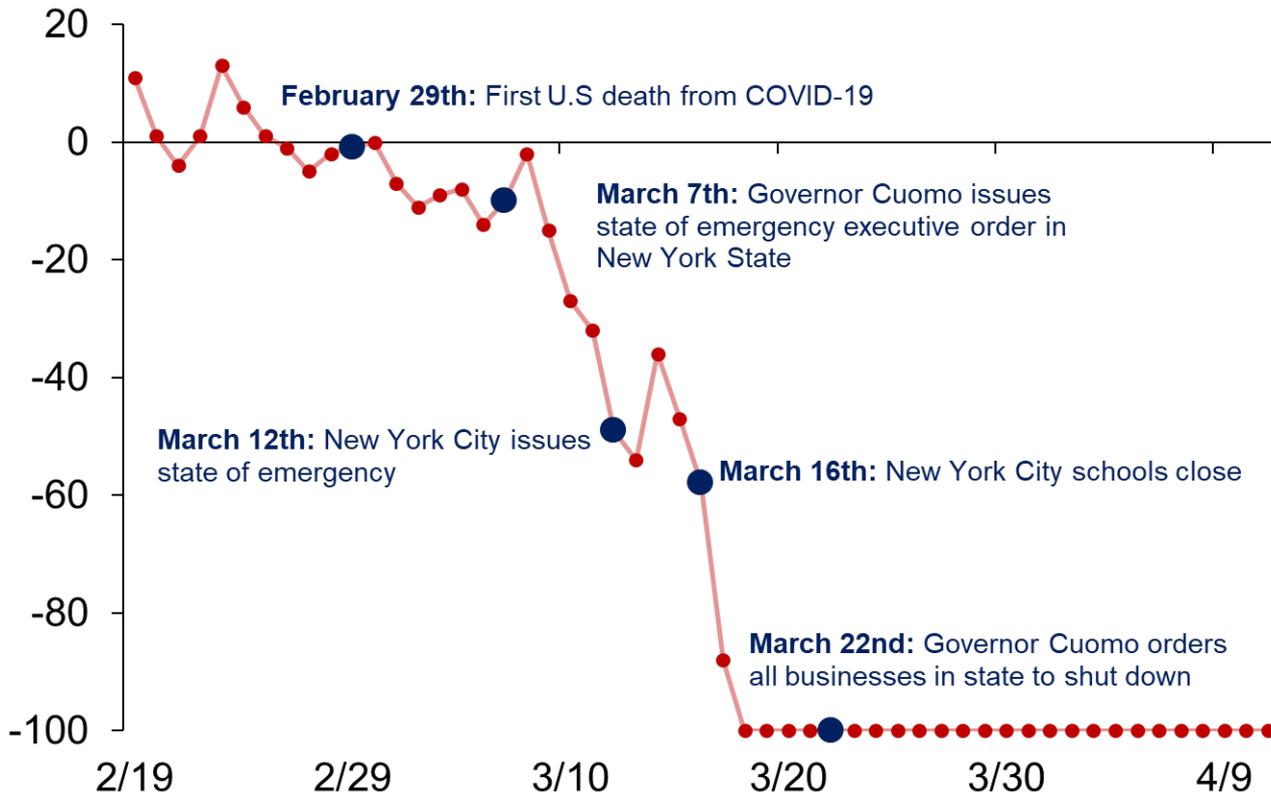


Source: Oxford Economics/FlightRadar24

Sudden stop in restaurant activity

US: Seated dinners in New York state restaurants

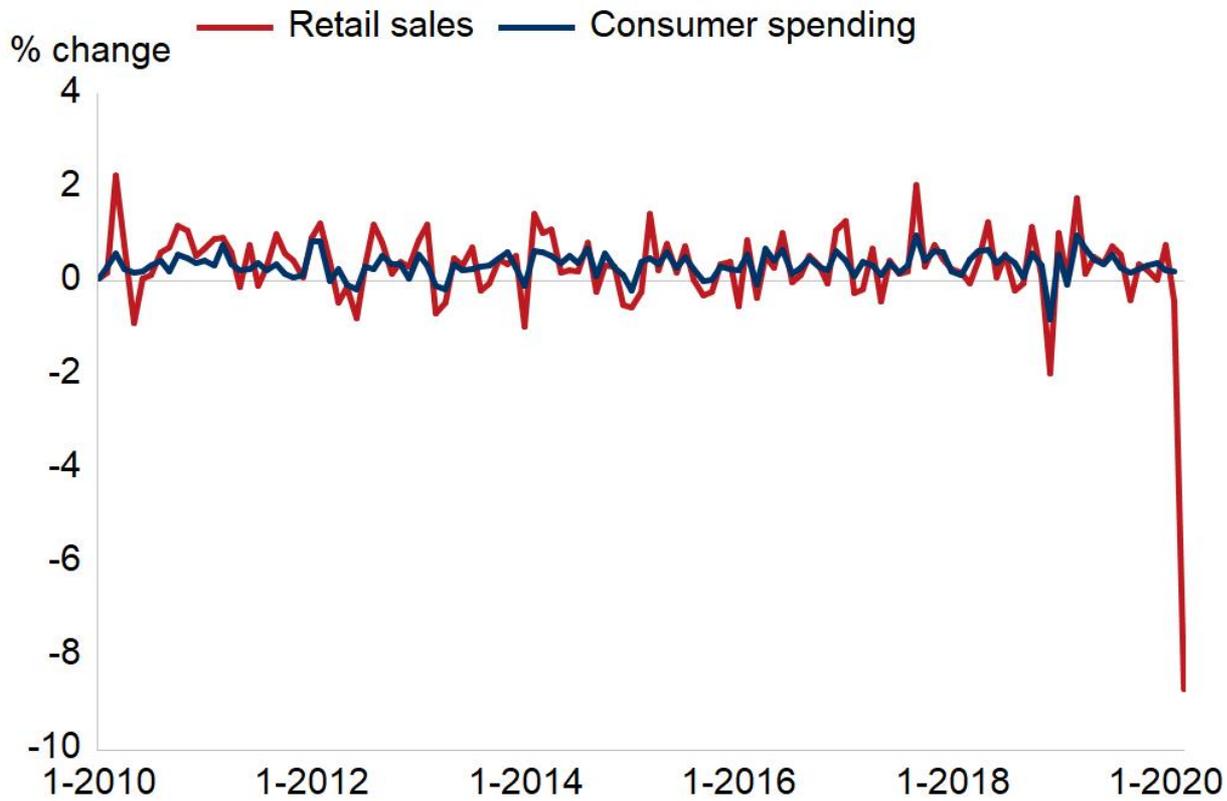
% change from one year ago



Source: OpenTable/NY.gov/Oxford Economics

Retail sales plunge by most on record in March

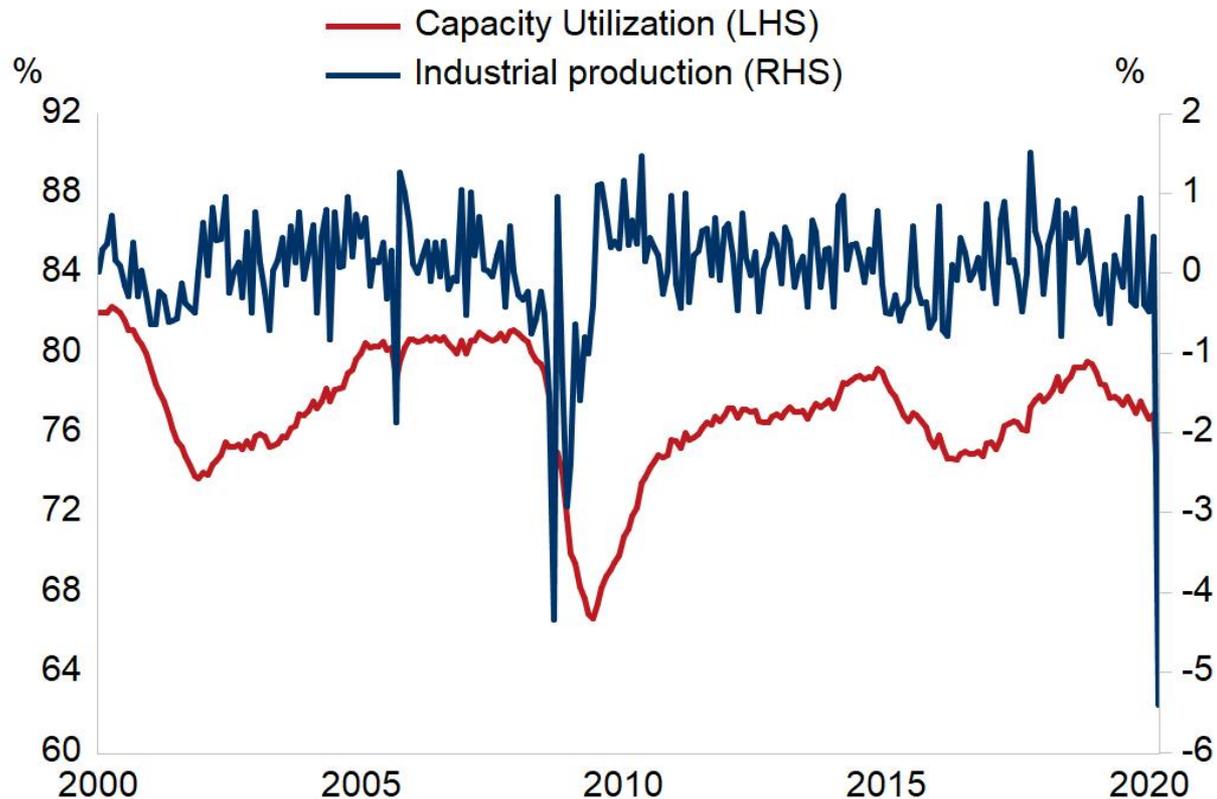
US: Retail sales



Source: Oxford Economics/Haver Analytics

Industrial activity suffers worst blow since 1946

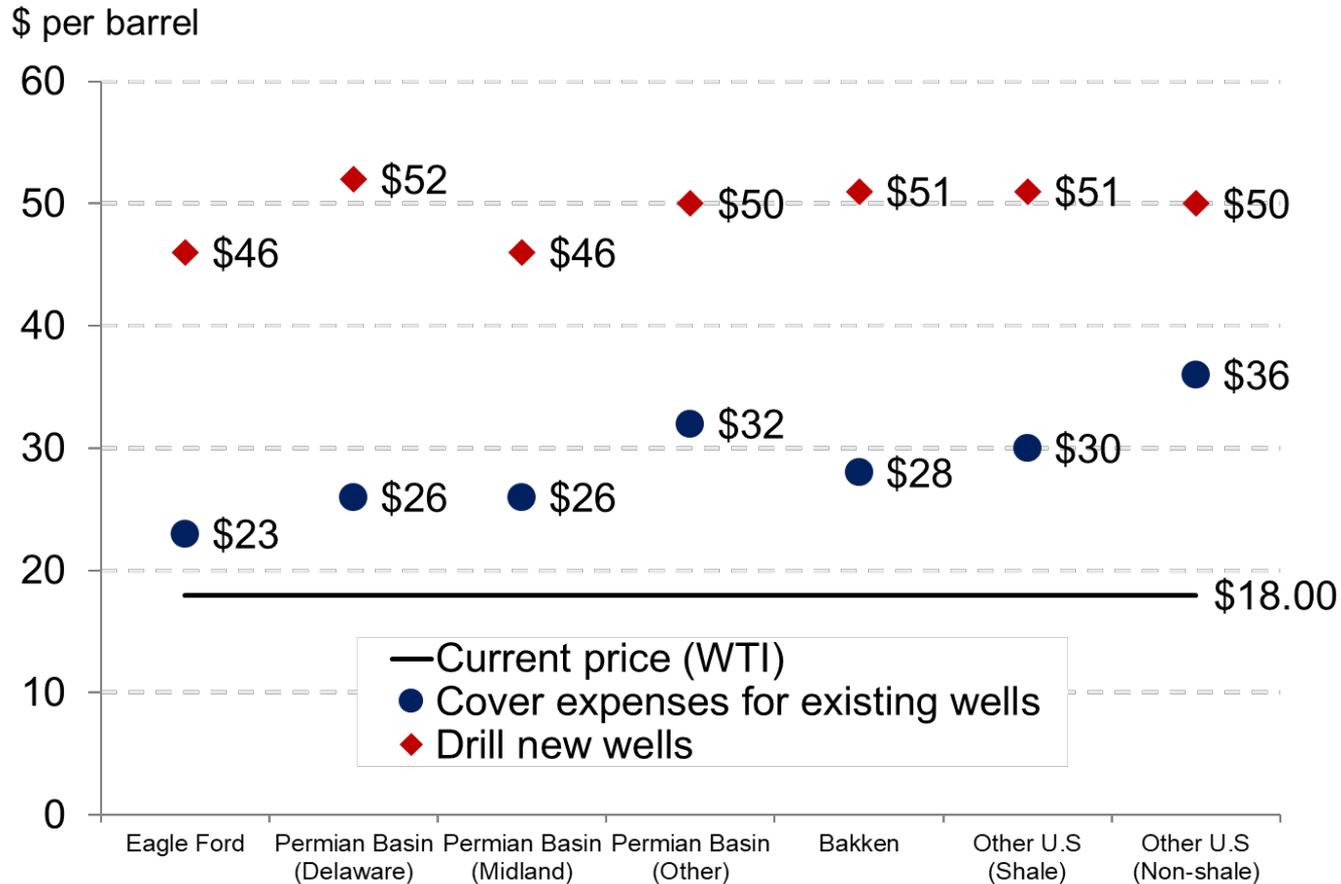
US: Capacity utilisation and industrial production



Source: Oxford Economics/Haver Analytics

Oil shock will leave a scar on shale sector

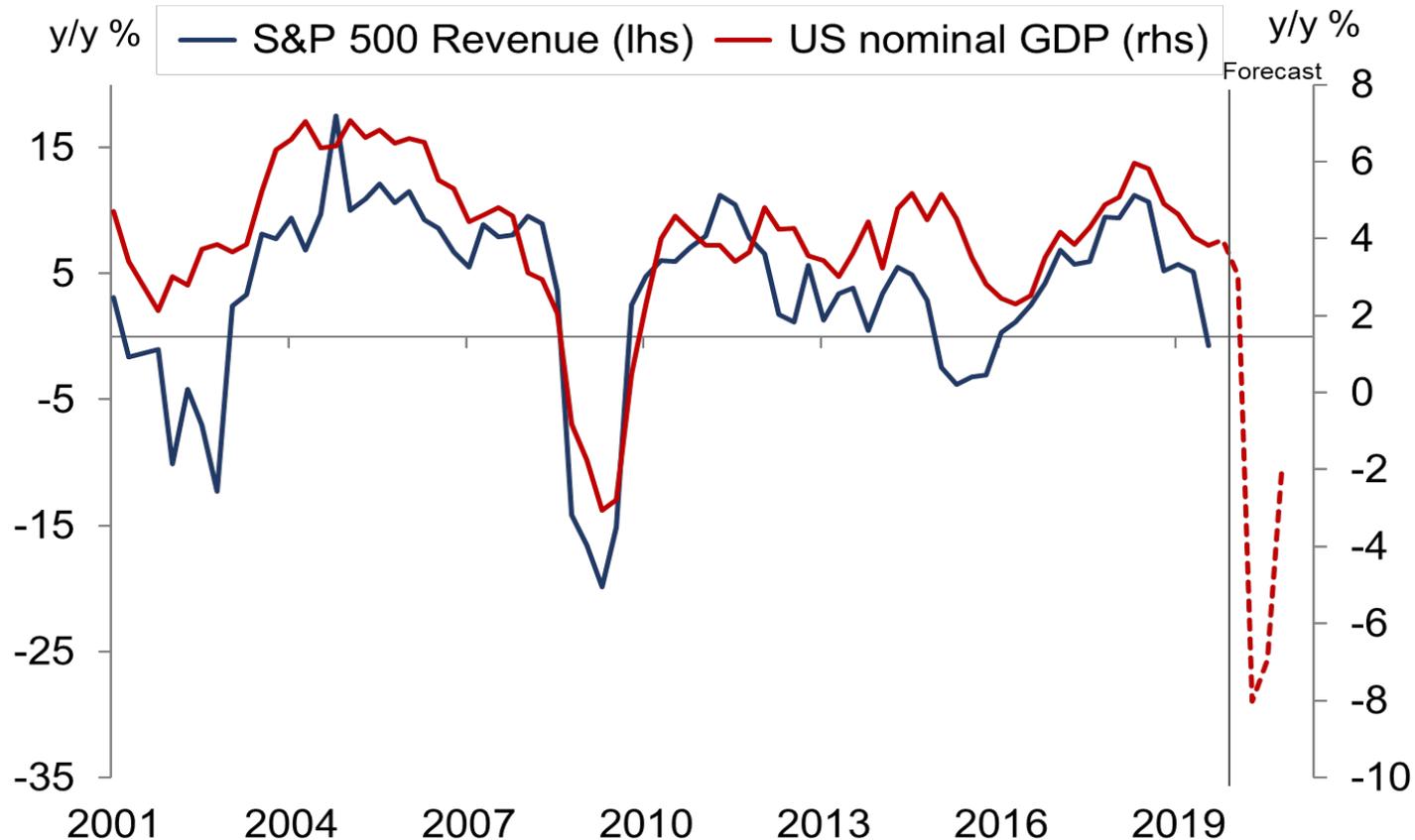
US: Average breakeven WTI oil price required to to:



Source : Oxford Economics/Dallas Fed/Bloomberg

Corporate profits poised to plummet

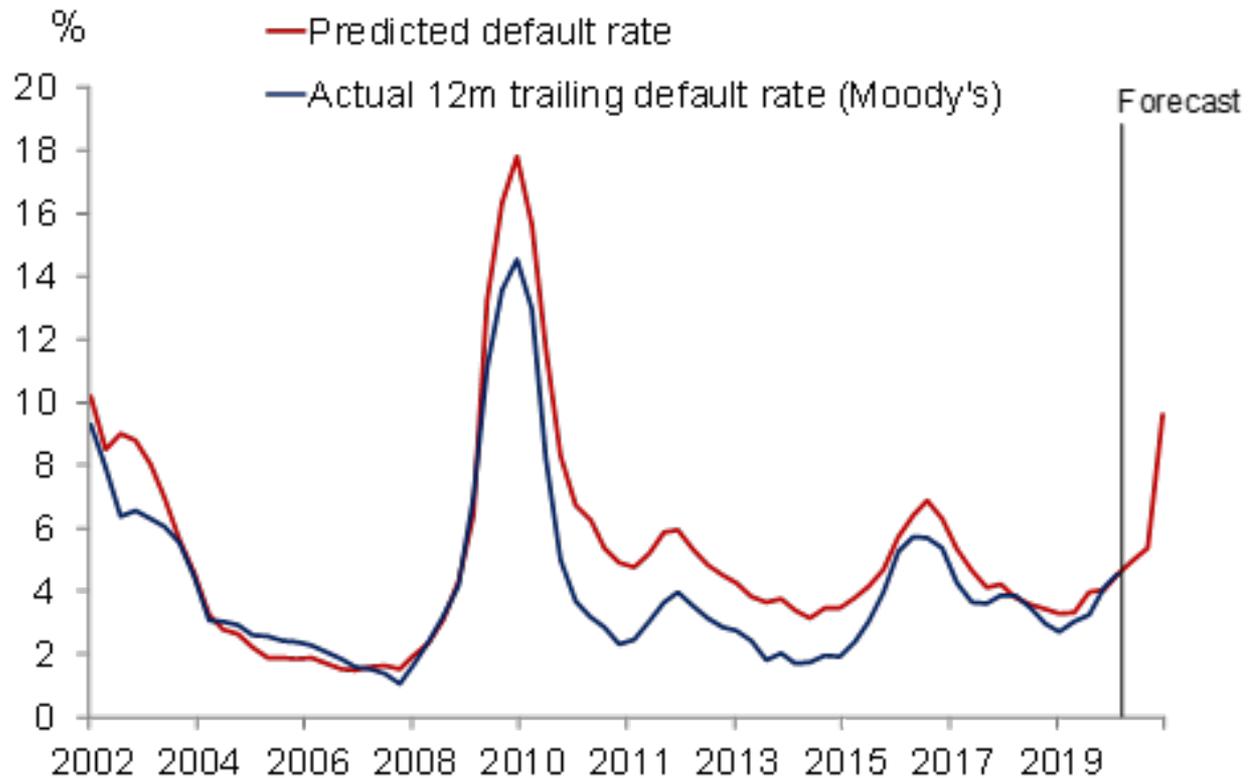
US: S&P500 revenues track nominal GDP



Source : Oxford Economics/S&P Global

Corporate bonds defaults set to jump

US: Speculative grade default rate

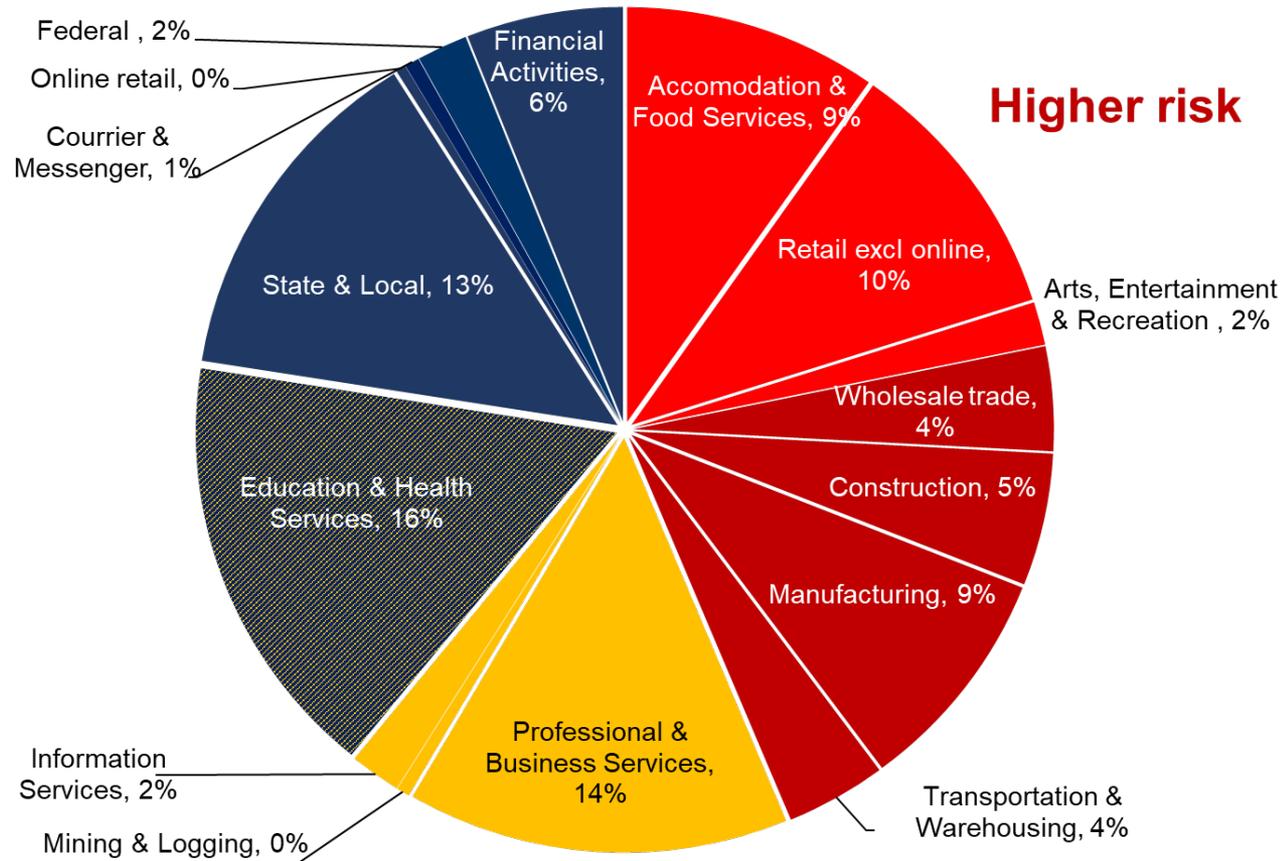


Source : Oxford Economics

An unprecedented labor market shock

The virus shock doesn't discriminate across sectors

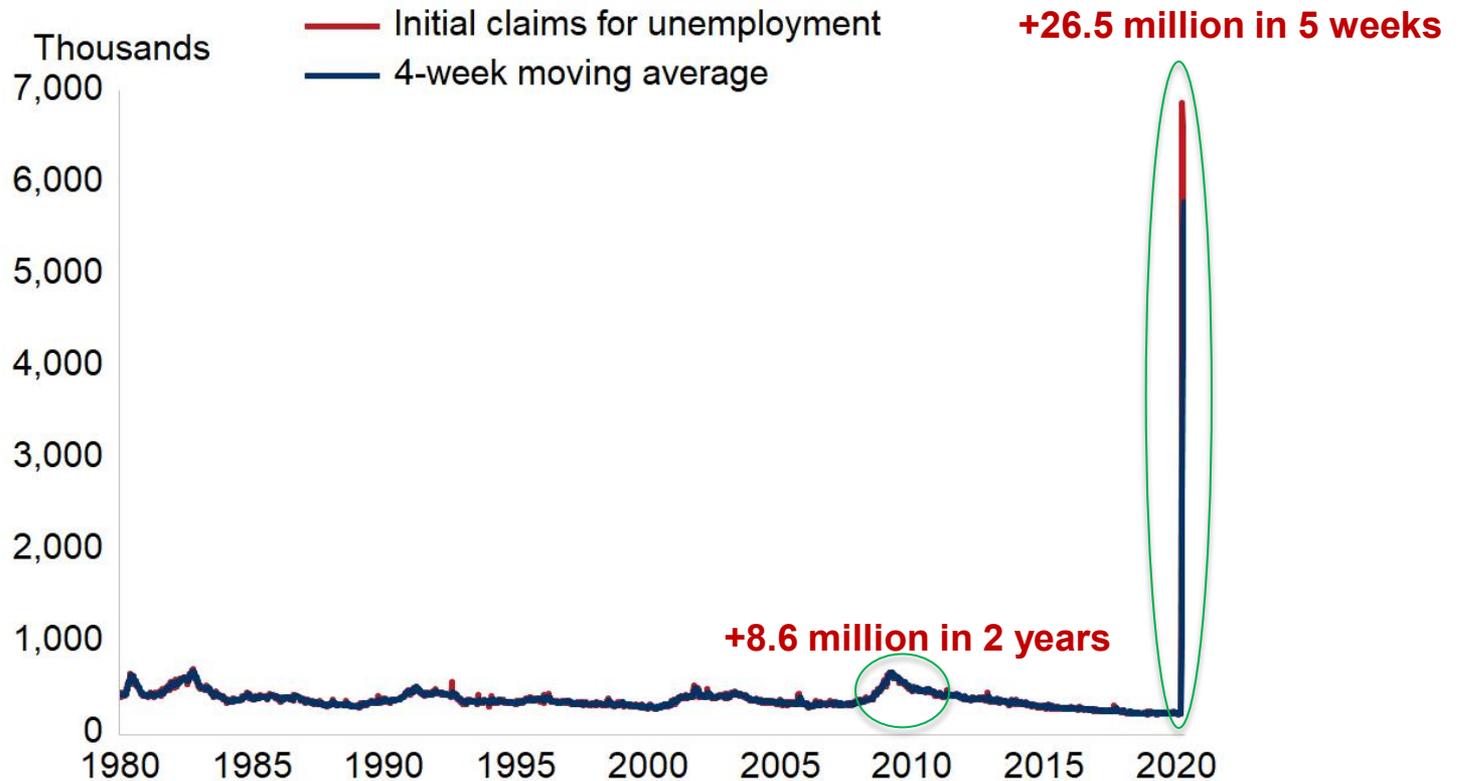
US: Employment at risk from virus



Source : Oxford Economics/Haver Analytics

Unemployment rate likely to surge above 15%

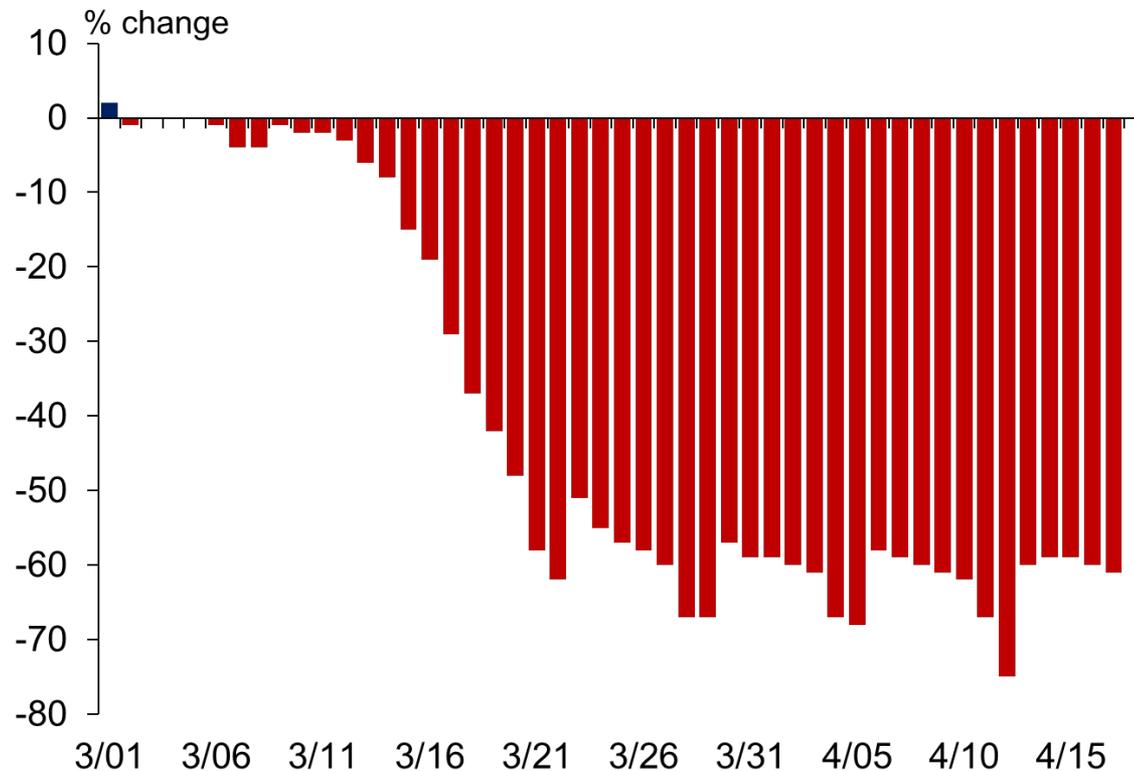
US: Unemployment claims



Source: Oxford Economics/Haver Analytics

Hourly employees are the worst hit

US: Hours worked by hourly employees



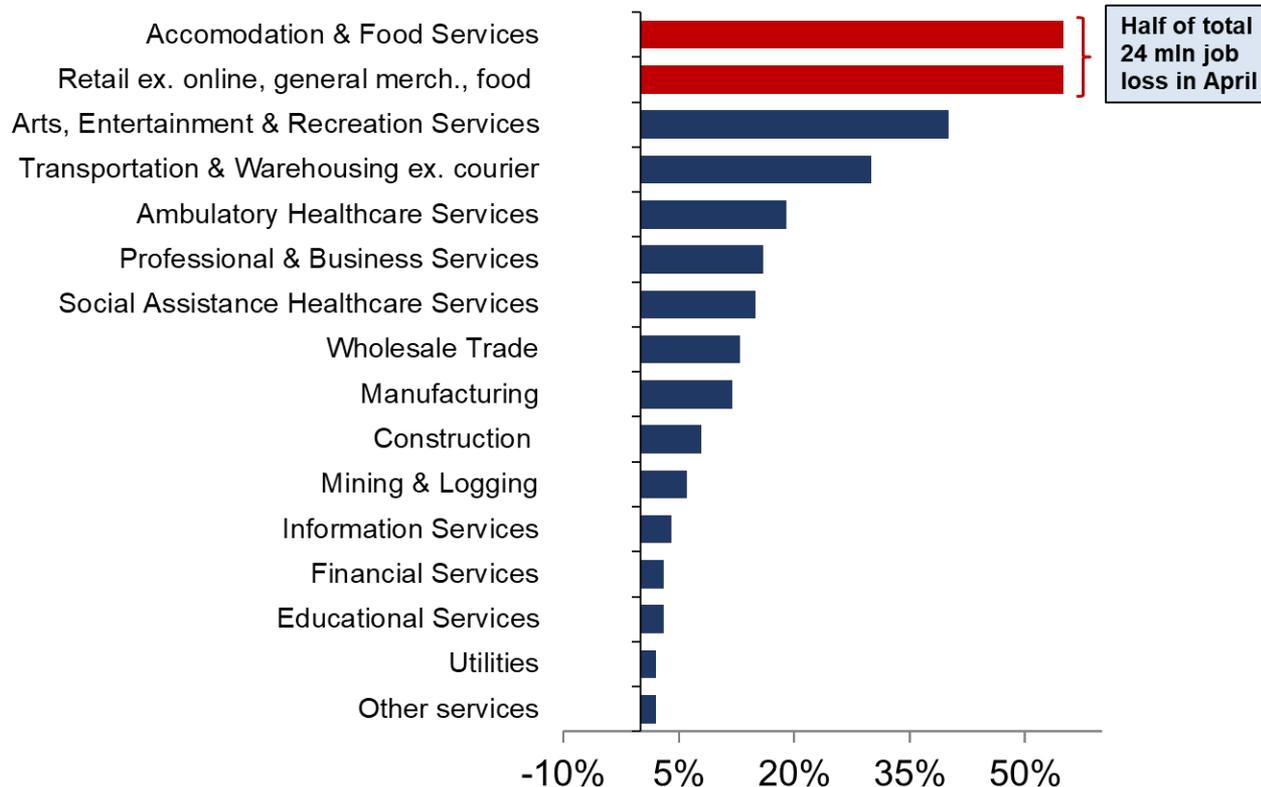
Source: Homebase/Oxford Economics

Hours worked in food & retail small businesses is down around 65% since January

We expect nearly 30mn total job losses

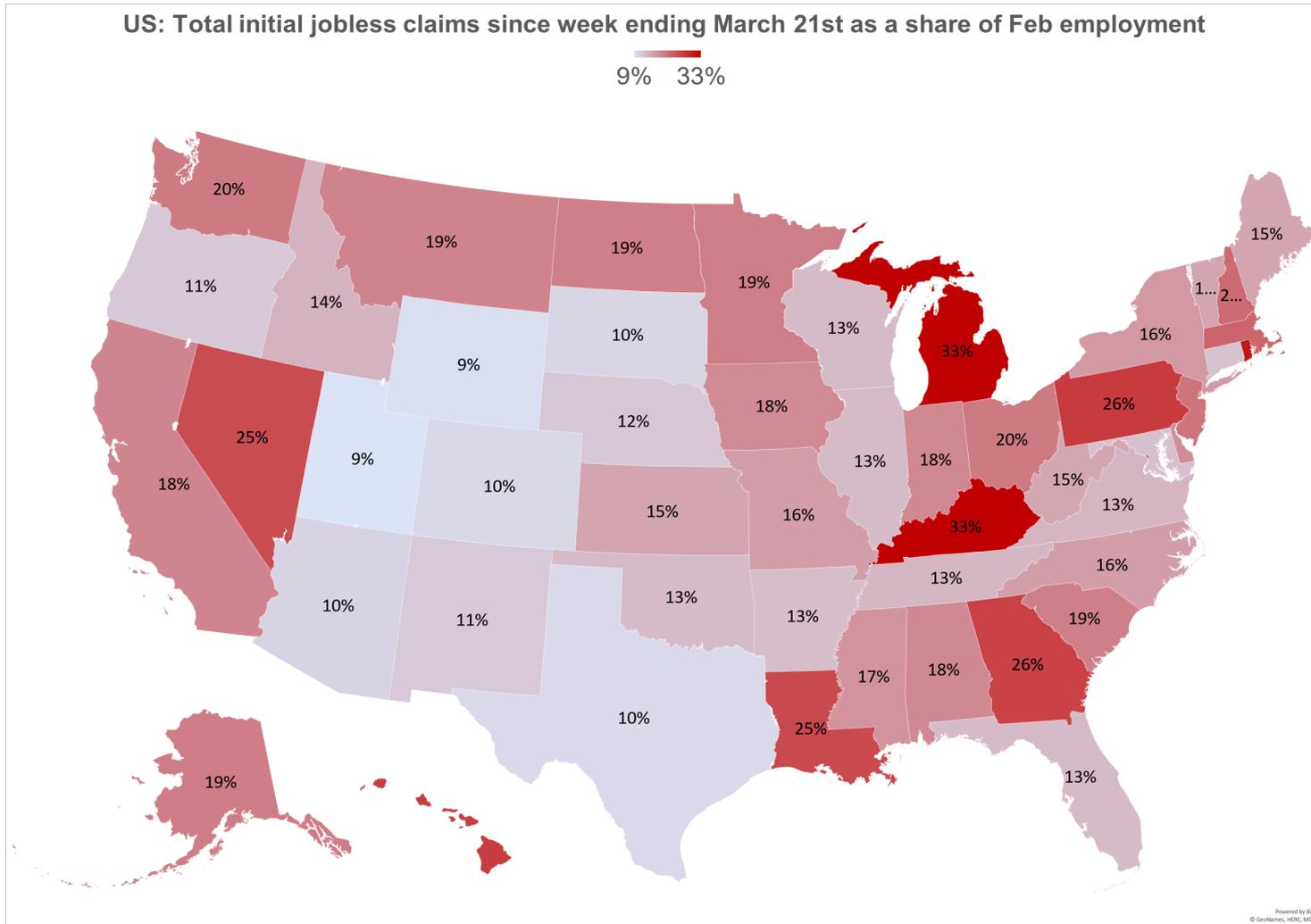
US: April expected job losses by industry

Job losses as a share of total industry employment



Source : Oxford Economics/Haver

And a soaring unemployment rate

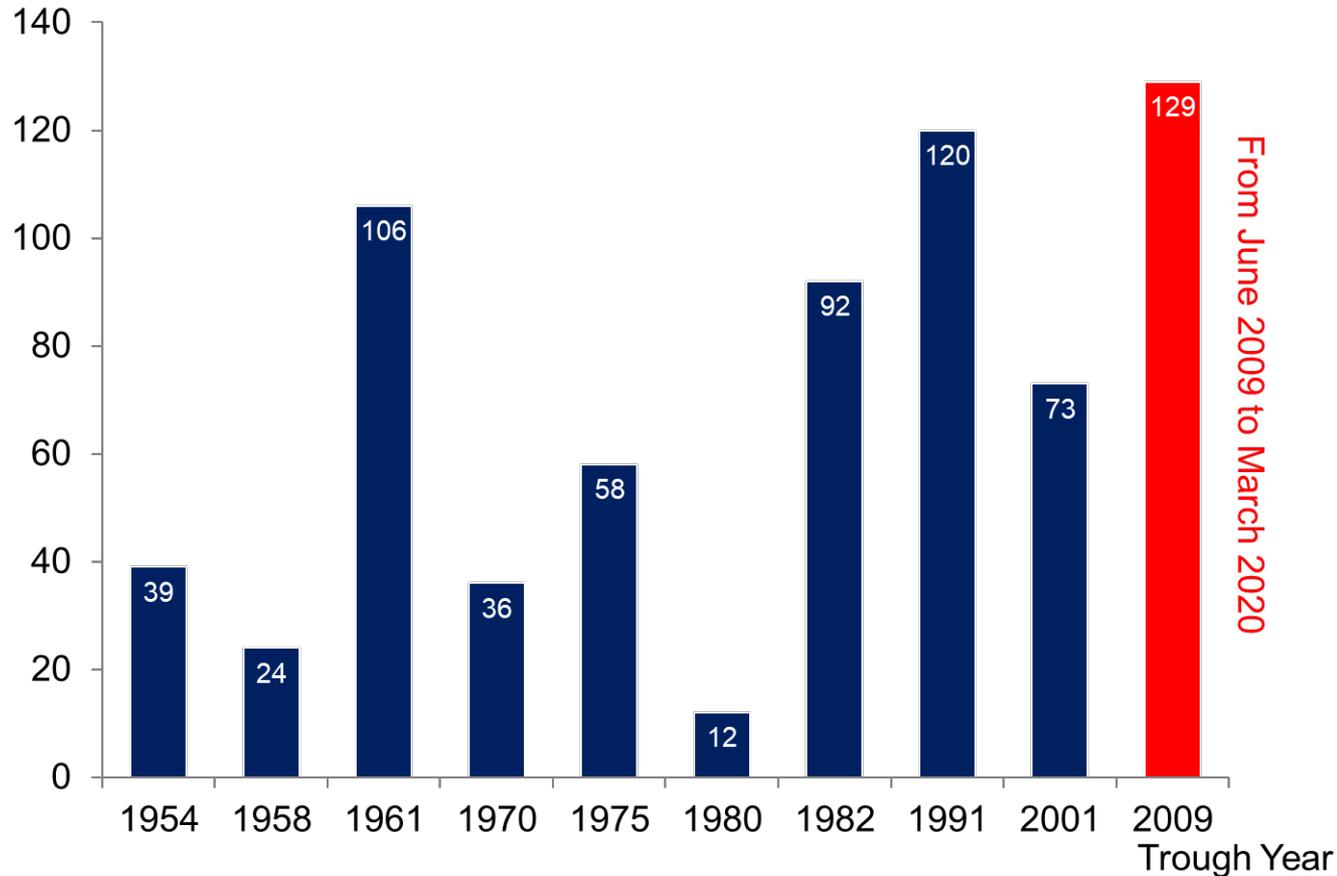


GCR puts an end to longest expansion ever

Longest expansion on record is over

US: The longest economic expansion on record

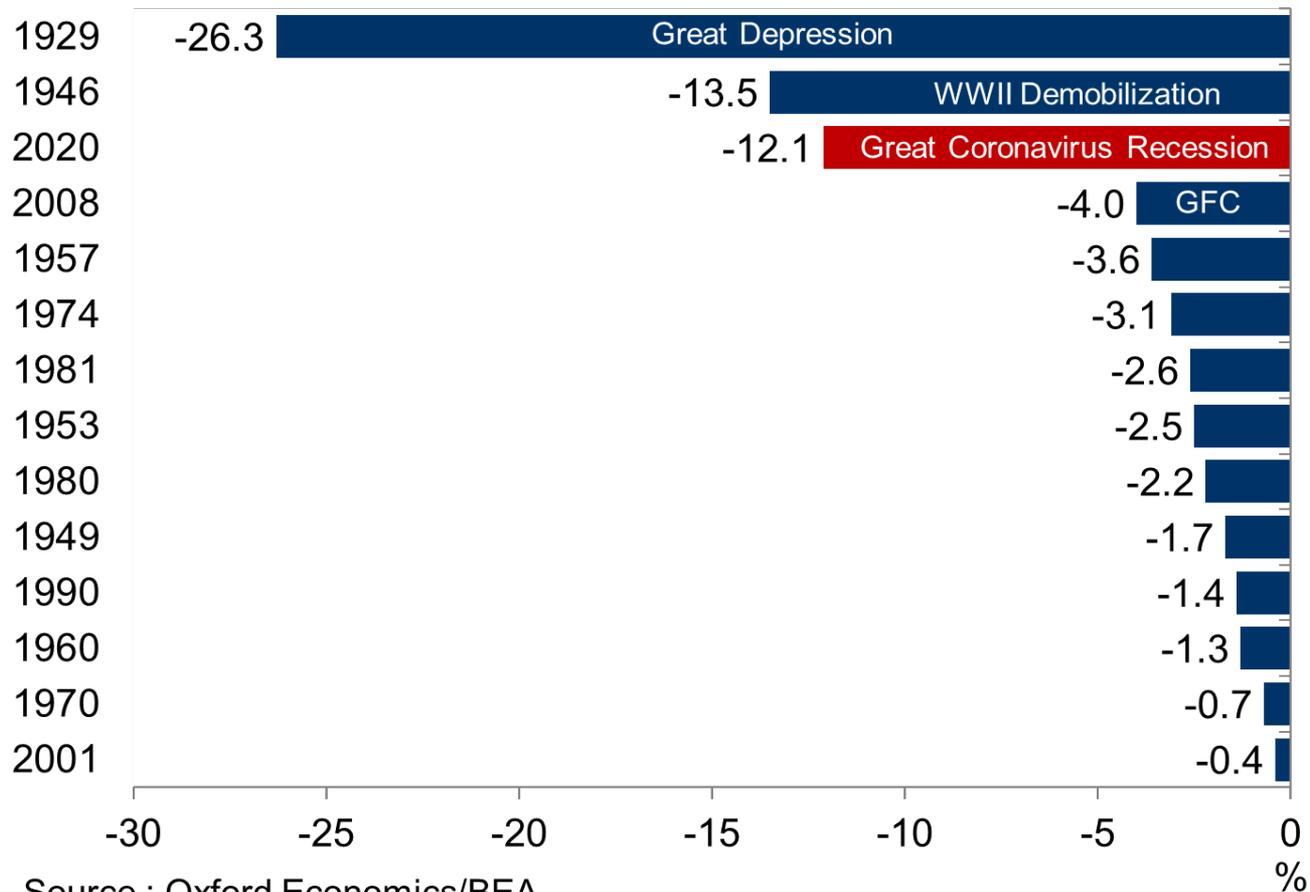
Number of months, Trough to Peak



Source : Oxford Economics, NBER

Sharpest drop in activity since WWII

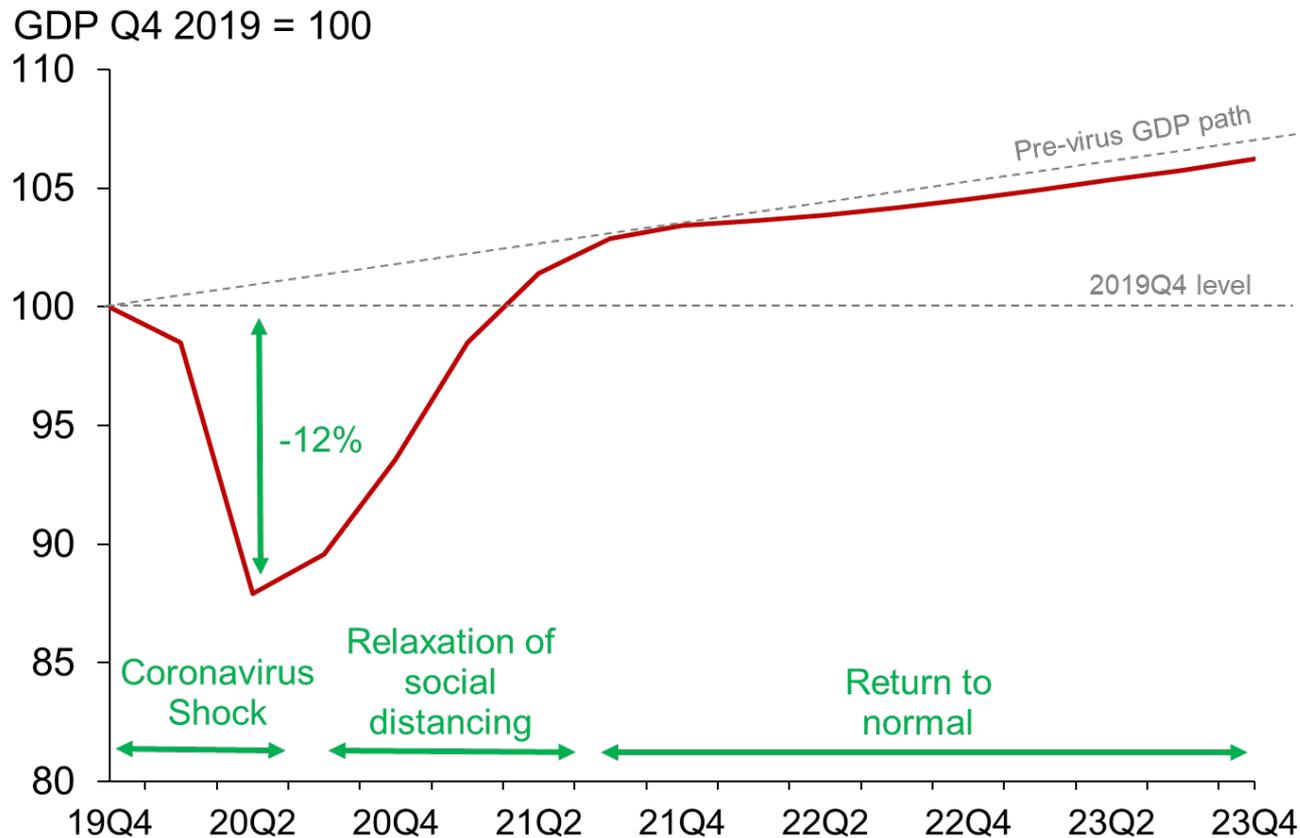
US: Cumulative GDP decline during recessions



Source : Oxford Economics/BEA

A severe contraction & a gradual rebound

Deepest economic contraction since 1946

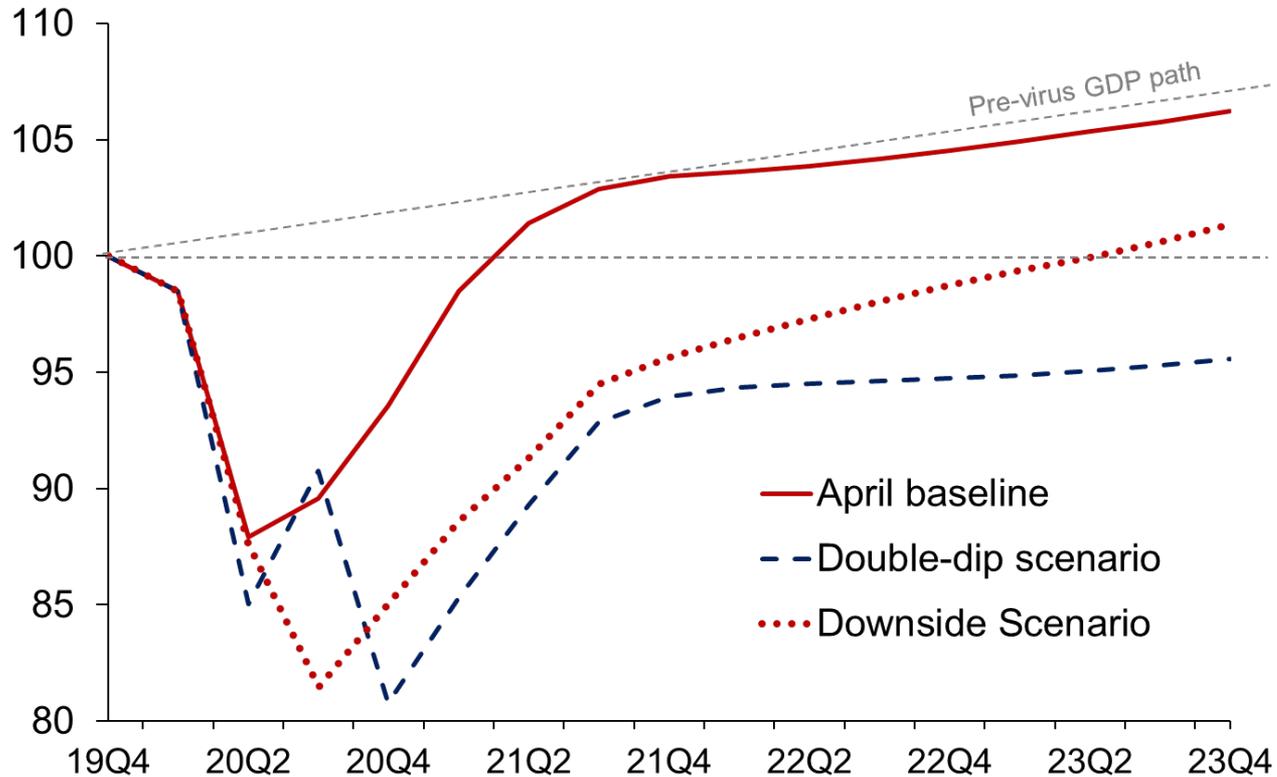


Source : Oxford Economics

With risks skewed to the downside

Second contagion wave leads to new lockdown

GDP Q4 2019 = 100



Source : Oxford Economics

Policy response has been swift & slow

Fed can now lever up liquidity facilities to \$4 trillion

Fed's emergency policy actions

Traditional policy tools and QE

1. Fed slashed the fed funds target rate to the effective lower bound via two intermeeting cuts
2. Relunched open-ended QE - start buying \$500 billion in Treasury securities and \$200 billion in MBS
3. QE becomes unlimited and add CMBS to asset purchases
4. Massively pumped up repo offerings
5. Provided forward guidance - rates remain low until closer to Fed's dual mandate
6. Cut the reserve requirement ratio

Lender of last resort - providing liquidity to financial institutions

7. Discount window borrowing rate lowered and term increased to up to 90 days
8. Lower pricing and extend terms on standing US dollar liquidity swap lines
9. Increase the frequency of swap line operations with original five central banks to daily from weekly
10. Establish temporary US dollar liquidity swap lines with wider group of central banks
11. Temporary FIMA Repo Facility
12. Intraday credit extended by the Reserve Banks
13. Revived the Primary Dealer Credit Facility (PDCF)
14. Temporary change to the supplementary leverage ratio rule - Treasuries and deposits exempt

Liquidity provider of last resort to credit markets

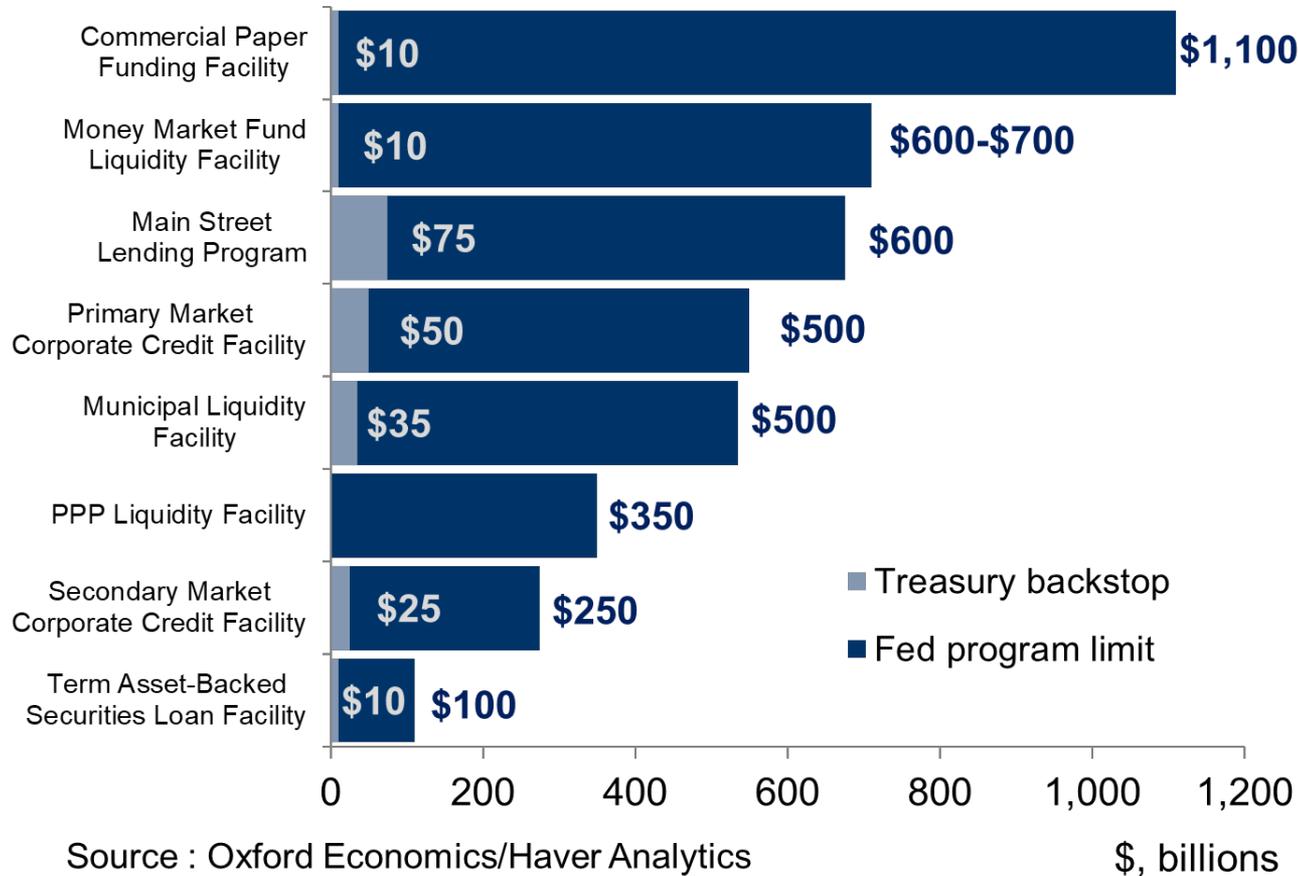
15. Revived the Commercial Paper Funding Facility (CPFF)
16. Established the Money Market Mutual Fund Liquidity Facility (MMLF)
17. Established the Primary Market Corporate Credit Facility (PMCCF) - support new corp. bond issuance
18. Established the Secondary Market Corporate Credit Facility (SMCCF) to buy corporate bonds
19. Increase the size and scope of PMCCF, SMCCF, and TALF - include BB- rated high yield debt
20. Revived the Term Asset-Backed Securities Loan Facility (TALF).
21. Municipal Liquidity Facility - buy short-term debt of state and local governments

Lender of last resort to main street

22. Paycheck Protection Program Liquidity Facility (PPPLF) - provide term financing backed by the SBA PPP loans
23. Main Street Lending Program - provide loans to small and medium-sized firms

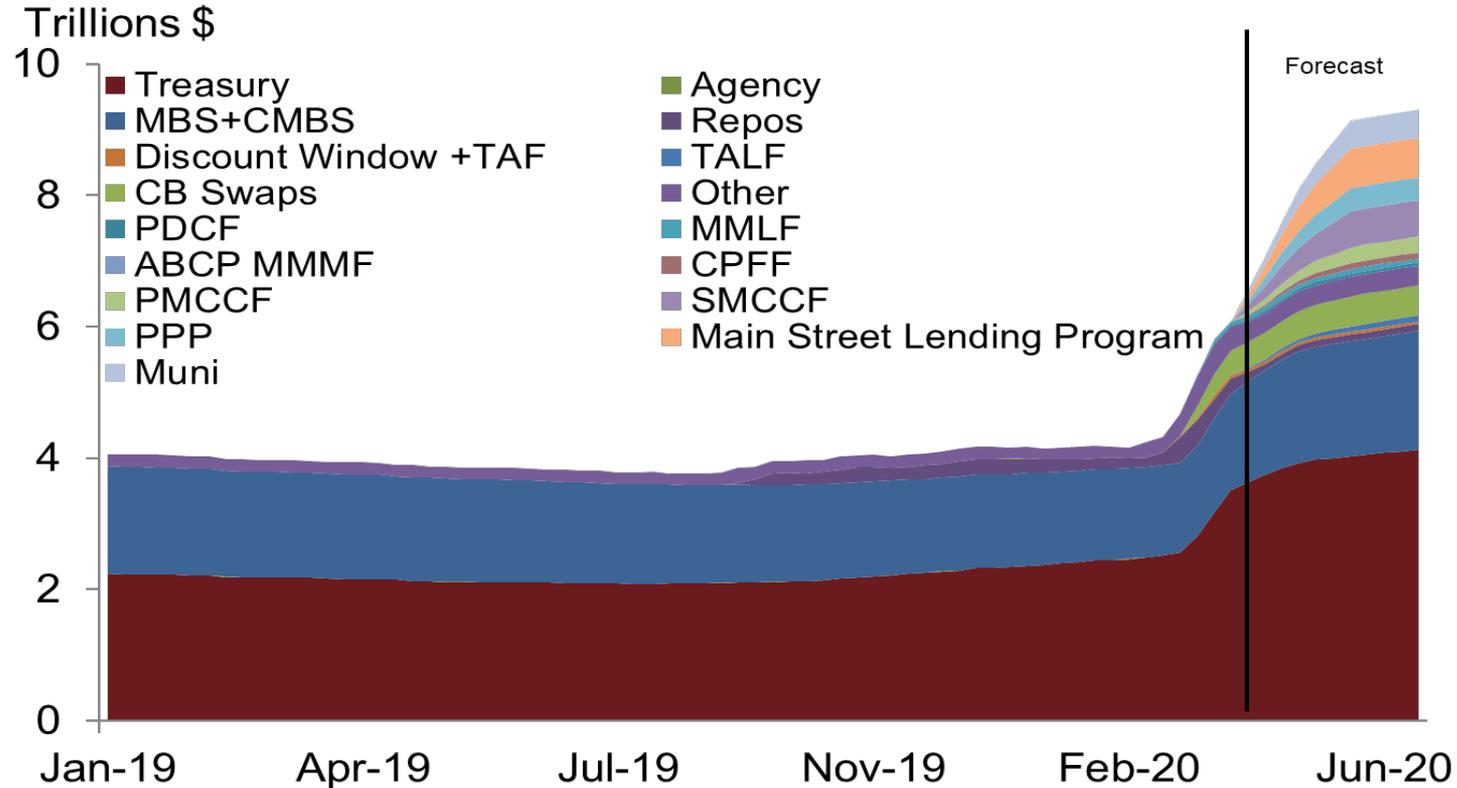
A perspective on the Fed's emergency programs

US: Fed's giant bridge loan



Balance sheet poised to double in size

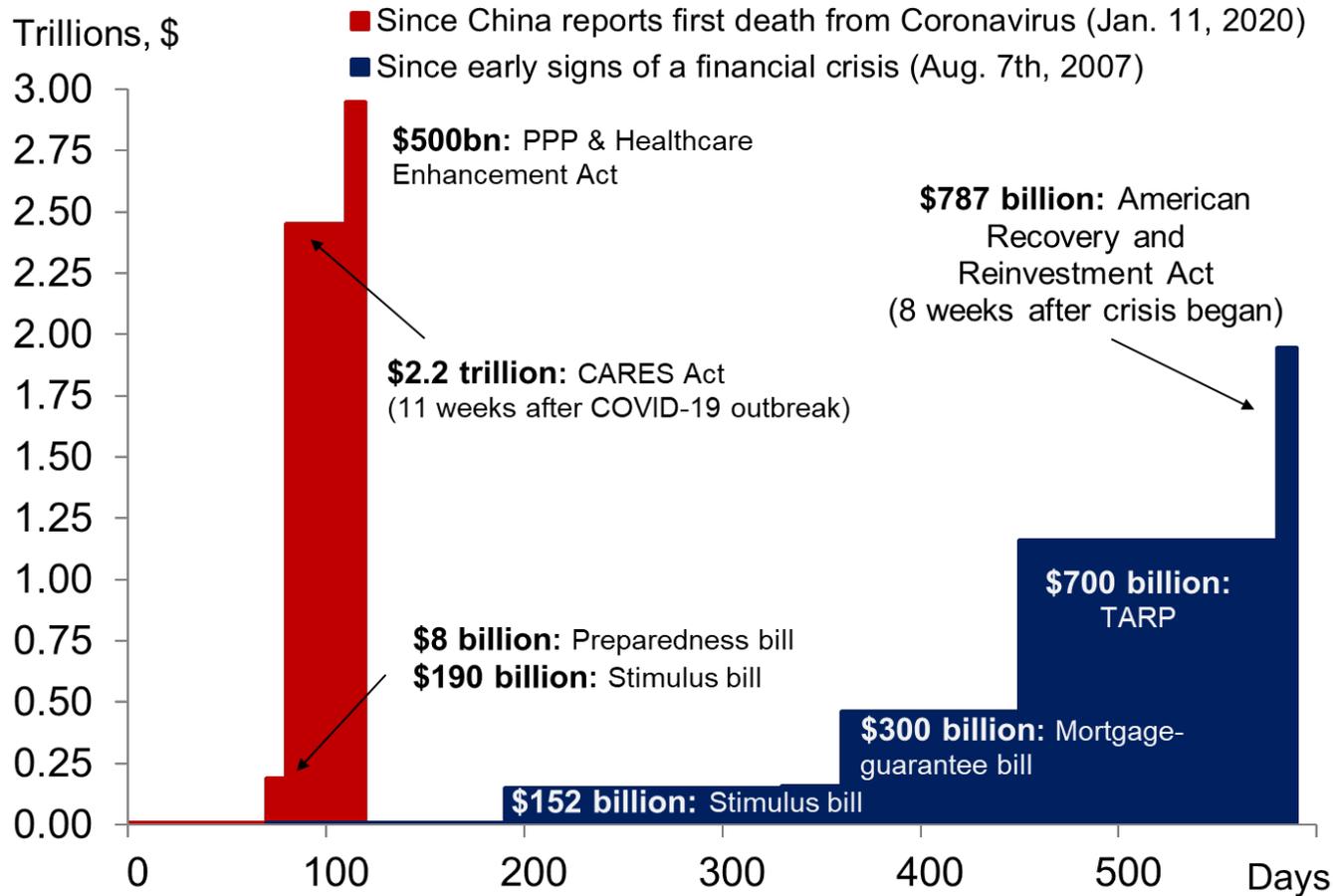
US: Fed balance sheet jumps to new record



Source : Oxford Economics/Haver Analytics

COVID stimulus in comparison to the GFC stimulus

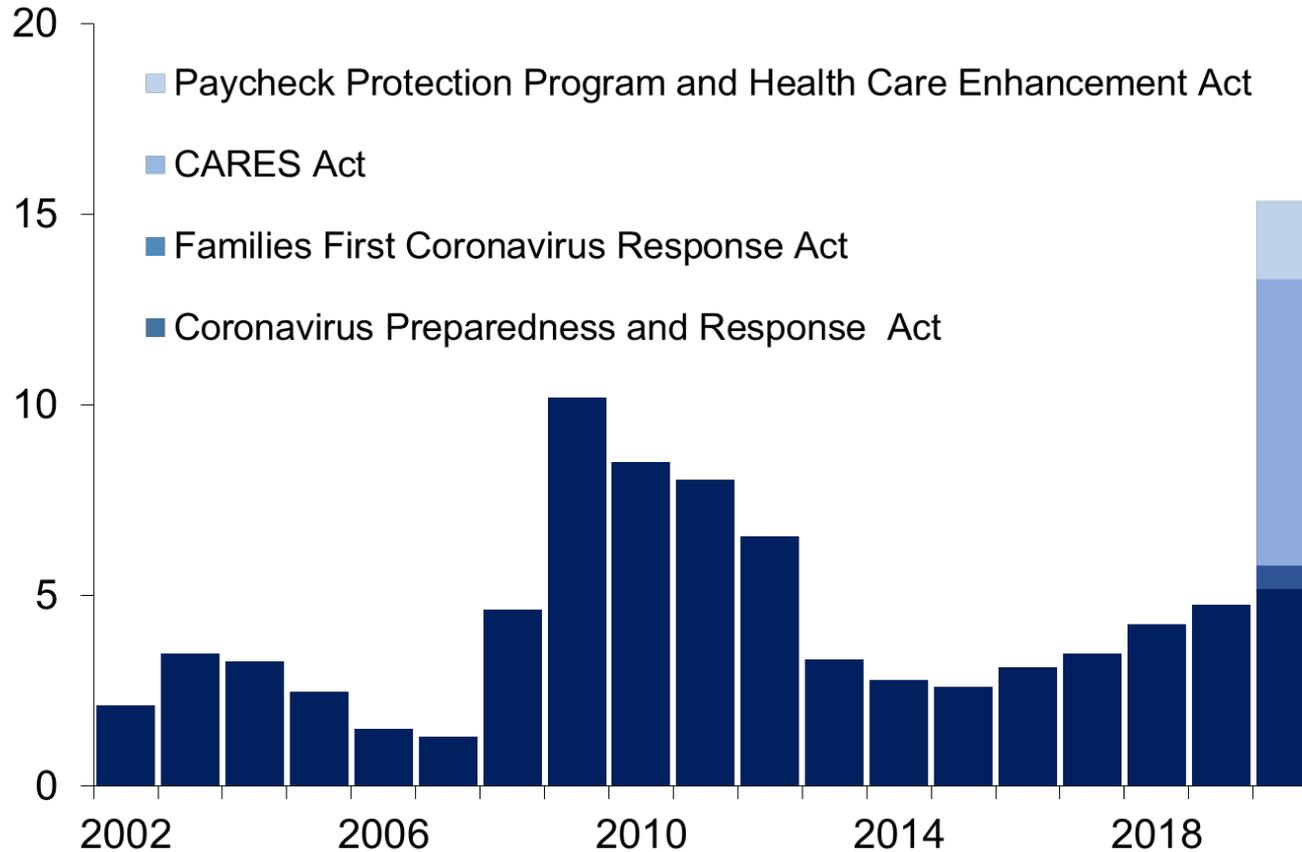
US: Funds authorized by Congress



Budget deficit set to triple in 2020

US: Deficit as a share of GDP

% of GDP



Source : Oxford Economics

Conclusions

Adapting to a new normal

- **Coronavirus shock** started as a supply chain shock for China, but it's rapidly transformed into a global demand, supply, confidence, oil & financial shock
- The cruel "**lockdown paradox**" is that the more severe the containment measures are, the faster we'll get past the virus, but the sharper the economic hit will be
- **Largest decline in activity and employment ever in Q2** as high frequency data indicate
- **Assuming 10-12 week lockdown** economy will shrink more than 4% in 2020
- **Financial conditions are acting as an amplifier**, and the risk from a liquidity or credit squeeze is real, especially in the context of elevated corporate debt
- **Fed emergency steps** won't stop the virus, but it is essential in ensuring the functioning of financial markets
- **Fiscal policy stimulus is large at 12-15% of GDP**, it will buffer the economy from a sharper downturn, but not prevent it.
- Shape of the **rebound is a function of the timing, severity, duration and effectiveness of the lockdown**, but we know it will be gradual and uneven.



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