

THE ECONOMIC OUTLOOK GROUP



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ECONOMIC TALKING POINTS

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The Economic Fallout From the Covid 19 Pandemic Has Begun

We have now entered the eye of this biological storm and, as expected, the economic fallout has been merciless. In just a matter of days, an obscure microorganism drove millions of Americans to quickly file for unemployment benefits.

After five years that saw weekly claims for jobless insurance hover below 300,000, new applications for such aid shot up to more than 3.28 million Americans. There is absolutely no historical precedence for this.



Some people, like Treasury Secretary Steve Mnuchin, have sought to downplay this surge by saying the latest numbers seeking unemployment benefits are “not relevant” because the \$2 trillion stimulus package better prepares individuals and

companies for the downturn. But that misses the point. The money that will flow from this mega-spending package is certainly comforting, but it won't materially change the course of the economy over the next several months and possibly much longer.

For example, we now have to brace ourselves for what will be the worst second quarter in US economic history. We are projecting economic activity will contract by 18% rate this spring — and even that ugly data point may be too optimistic. Some forecasters see the US economy plunging by more than 30% in the period!

Ironically, the bigger the drop in 2Q growth, the better the chance we can actually avoid another downturn in the summer quarter. The reason being that a horrific 2Q fall in GDP suggests that households and businesses are taking seriously the precautionary steps necessary to slow the spread of this highly dangerous virus. It means consumers were homebound and that businesses were either closed or functioned with skeleton crews. If that's the case, it would help hospitals and doctors better manage the treatment of those ill and also boost the morale of Americans as they receive some financial support from the stimulus package.

On the other hand, any suggestion by the White House that Americans can resume normal activity by April would be disastrous for the economy. Based on the latest medical data, Covid-19 is very contagious (with an R naught rating of 2, which means one person infects two and those two infect four, and so it escalates) and deadly (with a mortality rate of around 4% of those infected with this virus). If these numbers hold, Covid-19 would be even more fatal than the 1918 Spanish flu, which killed tens of millions of people around the world. (The 1918 Spanish flu had an R naught of 1.8 and a mortality rate of 2.5%.)

Keep in mind we are still far behind the curve in arresting this new virus. Should the Trump Administration ignore the advice of every medical expert on infectious diseases and prematurely call for businesses to re-open and people to return to work, it would dramatically increase the number of fatalities and further delay the economy's recovery.

If cooler heads prevail in the White House, the question then turns to how soon we might see economic activity return to normal again?

There is no easy answer at this time. Economic models are not structured to handle exogenous shocks like a pandemic. To come up with a credible forecast, we first need to know when the medical community can contain the spread of this pathogen. No economic stimulus can work if consumers remain seized with fear that they will contract the virus if they emerge from their homes.

Frankly, we found it odd so few funds in the three stimulus packages went to medical research that focuses on crushing the actual culprit that has paralyzed the global economy. The money flowing out of the government certainly helps companies remain viable and provides consumers with the resource to spend once conditions improve. But for conditions to genuinely improve, more money should have been allocated to those on the front lines working on a vaccine or other anti-viral medicines. Progress on that front would have to happen first before the economy can bounce back.

For that reason, our assessment of future economic growth depends on two key variables. When will the threat from the coronavirus subside enough to embolden people to leave their homes and resume work? And the second factor to influence future economic activity will be the outcome of the November elections, given the wide difference in policies between the two principal adversaries, Trump and Biden. At this juncture, any economic forecast for the next 12 to 18 months would have limited value. We first have to know when public health officials can express confidence that the danger posed by the coronavirus has receded.

Until then, fasten your seat belt for what is certain to be a period of extreme economic turbulence ahead.

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