1Q20 Economic Summary

After a promising start to the year, things changed drastically when the COVID-19 pandemic began to wreak havoc across the globe. As the devastating economic impact of the virus became apparent, the Federal Reserve slashed the fed funds rate, and treasury yields plummeted across the curve as investors sought safe-haven assets. Equity markets, which hit record highs in January and February, ended the quarter down more than 20%, culminating in the worst quarter for stocks since the financial crisis.

The coronavirus first appeared in late December in the city of Wuhan in China's Hubei province. By late January community spread was accelerating and Wuhan was placed under quarantine with the entire province of Hubei following shortly thereafter. At first it was believed the virus, dubbed COVID-19, was relatively contained in China but by mid-February outbreaks were reported in South Korea, Iran, and Italy. By mid-March the World Health Organization (WHO) declared COVID-19 a pandemic, and the US declared a national emergency as the virus began to rapidly spread across the country. By the end of March, approximately 1/3 of the globe was under some form of lockdown, and global economic growth had ground to a halt.

In January the IMF was forecasting 3.3% global GDP expansion for 2020. However, after the pandemic crushed demand for goods and services around the world, the organization is now forecasting the global economy will contract by 3% this year, likely resulting in the worst global recession since the Great Depression. China is expected to report its first quarterly decline in growth since it began tracking quarterly GDP in 1992. Although China began to re-open factories in March, trade is expected to remain weak as the countries that consume most of China's exports remain in lockdown. Given its export heavy economy, Europe is also expected to be hit hard by the pandemic, particularly in Italy and Spain which have surpassed China in terms of death and infection rates from the virus. Japan's economy is also expected to contract as the outbreak has disrupted production and exports. In addition, although Japan has so far avoided imposing nationwide travel and work restrictions, public sentiment is expected to have deteriorated significantly after the postponement of the 2020 Summer Olympics.

Although the US is not as heavily reliant on exports as other countries, the coronavirus has crippled the economy nonetheless. While the US has not been immune from the supply chain disruptions and demand decreases that have impacted manufacturing worldwide, it's the hit to the services sector that is expected to deal the most crushing blow to economic growth. Services account for approximately 70% of US GDP and have been the stalwart for growth during the expansion. However, with the majority of states imposing shelter-in-place orders, consumer spending on things like transportation, entertainment, restaurants and retail has dropped off dramatically. The lockdown has prompted mass waves of layoffs, resulting in a surge in unemployment. Nonfarm payrolls dropped 701,000 in March and the unemployment rate jumped to 4.4%. Unfortunately, the March data doesn't fully represent the damage the coronavirus has done to the jobs market. The nonfarm payroll survey was taken in the first half of the month, before many of the government mandated shutdowns began, so it did not capture the nearly 10 million people who filed for unemployment in the last two weeks of March. Economists are forecasting that the unemployment rate may reach as high as 15-20% during the second quarter. It's a far cry from the employment picture just a month prior when the unemployment rate was near a record low and employers were having difficulty finding qualified workers.

With the world in an economic tailspin, central banks across the globe jumped in with emergency actions to ease monetary policy. The US Federal Reserve was no exception. When the Fed's surprise 50 basis point rate cut on March 3rd did little to calm financial markets, the central bank pulled out all stops on March 15th. The Fed slashed the fed funds target rate another 100 basis points to a range of 0.00-0.25%, launched at least $700 billion in quantitative easing, and announced multiple other measures to support the credit needs of households and businesses. In addition, in coordinated action with other central banks, the Fed announced it would boost dollar liquidity by increasing the frequency and duration of its currency swap operations. It was the largest single day set of moves the Fed has ever taken, but it was not done. Over the following few days, the Fed also introduced a slew of programs to ease pressures in short-term funding markets and to ensure financial market functionality. These programs appear to be working, but it will be quite some time before we see normalcy return to financial markets.

Knowing that it was going to take more than extraordinary monetary action to combat the economic carnage dealt by the health crisis, the US government did its part by signing into law a $2 trillion stimulus package on March 31st. It is the largest emergency aid package in US history and is aimed at helping American workers, small businesses and industries facing economic hardship as a result of the pandemic. While the package is massive and far-reaching, many believe more will need to be done to stave off a recession.

The COVID-19 pandemic has likely brought the longest economic expansion in US history to an end. The question now is how long and how deep will the recession be? The magnitude and speed of the economic collapse was unprecedented, and unlike other recessions it was spawned by a health crisis, not an unhealthy economy. As a result, monetary and fiscal policy can only do so much. The recovery will depend on how quickly the virus can be contained and when the world can reopen for business.