The Impact of the Coronavirus Outbreak on the Economy and Your Investments

The recent coronavirus outbreak has already enacted a human cost. At the time of writing, there have been nearly 4,700 confirmed cases, resulting in more than 100 deaths. Both numbers are expected to climb as healthcare officials around the world continue to monitor the situation. Calculating the economic impact of the outbreak, however, may be more difficult. Even If the outbreak does not turn into a widespread pandemic, it has the potential to roil the financial markets, and depending on the size of the outbreak, could spark a major sell-off and hinder economic growth.

In the immediate future, we anticipate increased volatility in the market. The market typically does not react well to uncertainty. Every new piece of information released or news story posted has the potential to cause a knee jerk reaction as investors panic and flee the market. On Monday, the S&P 500 index and Dow Jones Industrial Average both closed down 1.6 percent. The Nasdaq Composite fell 1.9 percent. Commodities were also hit hard, with oil falling more than 1 percent as China put several cities under a travel lockdown.

The broader economic impact will depend on the ultimate severity of the outbreak. Health officials have likened the coronavirus outbreak to the Severe Acute Respiratory Syndrome (SARS) outbreak from 2002 which killed 800 people over six months. The SARS outbreak is estimated to have cost the global economy $40 billion. Of course, a more severe epidemic would have greater consequences. The 1918 Spanish Flu pandemic infected 500 million people worldwide and killed as many as 50 million. A 2006 study from the U.S. Congressional Budget Office found that a similar event could cut U.S. GDP by 4.25 percent. The World Bank estimates that a global pandemic today could kill as many as 71 million and drop global GDP by 5 percent.

China, as the epicenter of the outbreak, may be hit the hardest. The Chinese economy is already growing at the slowest rate in decades and has become increasingly reliant on consumer spending to maintain growth. Wuhan, the city where the outbreak began, is an important tourist destination for China. The city saw 319 million tourists last year and has a GDP of $224 billion, accounting for 1.6 percent of China's total GDP. Depending on the duration of the lockdown, the outbreak could severely hinder China's already struggling economy. More than 300 Fortune 500 companies have operations in Wuhan, so Western corporations will suffer if consumer sentiment turns negative and workplace absenteeism grows.

The ultimate scope and scale of the outbreak—and the ensuing panic—cannot be predicted, but it can be prepared for. Stocks from airlines, hotels, movie theaters or any enterprise that relies on patrons traveling or congregating in large groups become much riskier in the immediate future. Investors will flock to the relative safety of secure, high-quality investments such as U.S. Treasuries. In fact, Monday's aforementioned losses in the stock indexes were matched by an increase of a similar percentage in U.S. Treasuries. Gold also saw a big increase as investors looking for a safe haven turned to it. Proper portfolio construction cannot eliminate the risk that a global pandemic would pose, but it can help to mitigate it. In times like these, the biggest mistake an investor can make is acting out of fear or anxiety. If you have any questions or concerns about your portfolio and its ability to weather this storm, please contact us to speak with an advisor.