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Coronavirus and the U.S. Economy

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Any opinions expressed here are my own and do not necessarily reflect those of the Federal Open Market Committee.

Introduction

Key themes

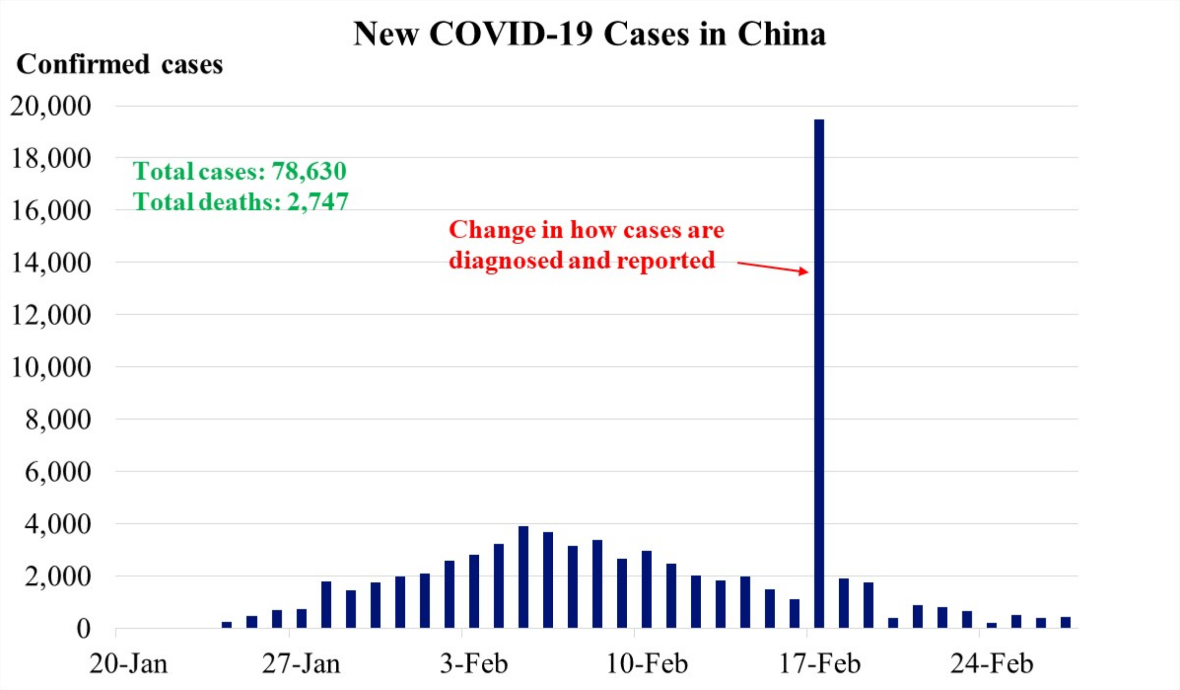
- Coronavirus (COVID-19) cases appear to be stabilizing in China, with additional cases being reported globally.
- Global economic growth is likely to slow temporarily, with much of the slowdown centered in Asia.
- The Federal Open Market Committee (FOMC) is in a good position because of previous policy rate cuts designed to insure the economy against adverse shocks.
- Longer-term U.S. interest rates have been driven lower by a global flight to safety, likely benefiting the U.S. economy.
- Further policy rate cuts are a possibility if a global pandemic actually develops with health effects approaching the scale of ordinary influenza, but this is not the baseline case at this time.

COVID-19 Outbreak

An unfolding human tragedy

- COVID-19 is the source of an unfolding human tragedy.
- The coronavirus case data are fast moving and subject to revision.
- The best information we have seems to suggest that confirmed cases in China are growing at a slower rate in recent days, and therefore the spread of the disease may be stabilizing there.
- Other countries have reported new cases in recent days.

Cases in China are growing at a slower rate



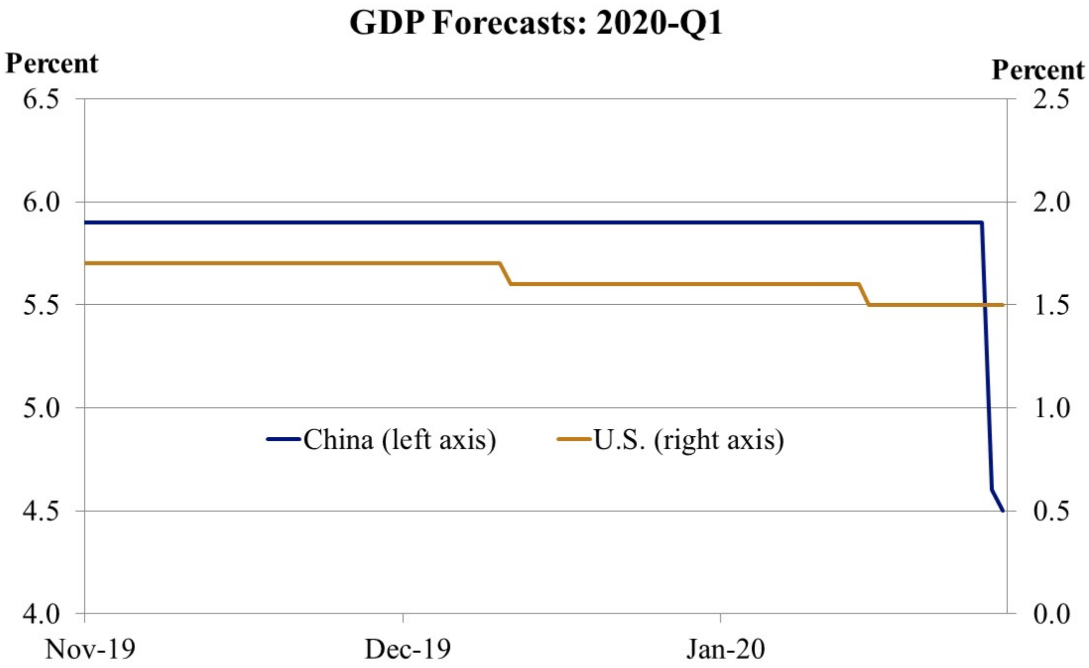
Source: World Health Organization COVID-19 Situation Reports. Last observation: Feb. 27, 2020.

Temporary Slowdown in Global Growth

COVID-19 effect on economic growth

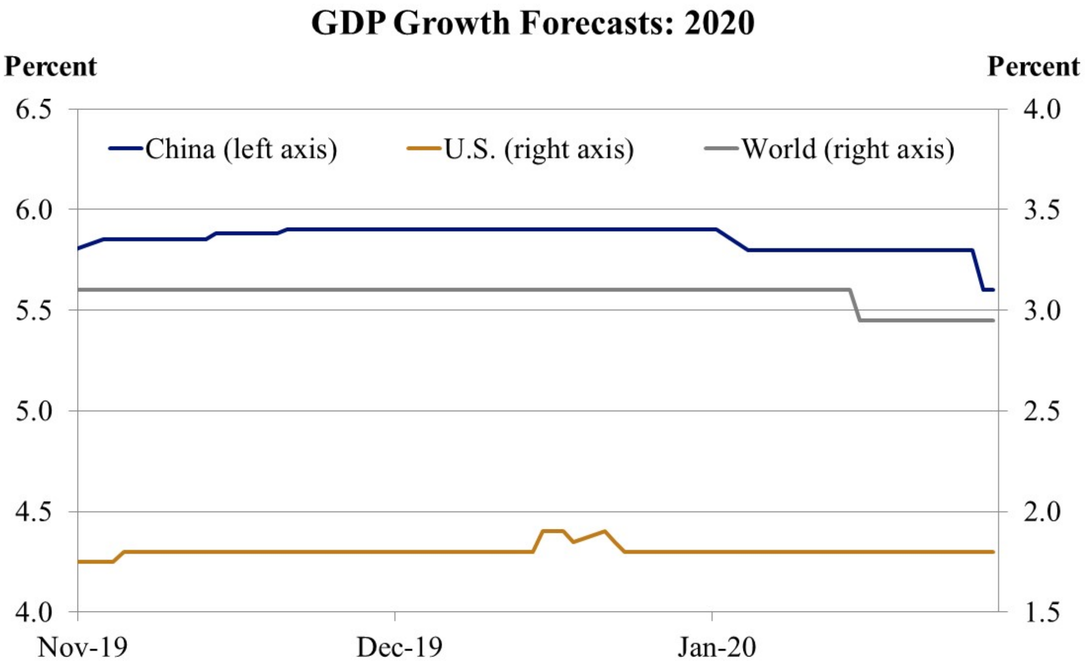
- There is likely to be a noticeable impact on Chinese GDP growth in the first quarter due to the coronavirus.
- Other countries may also be impacted directly by the virus, but these effects will likely be on a smaller scale.
- Temporary disruptions to global supply chains are likely to have ripple effects across the global economy.

China: Large downward revision for Q1 growth



Source: Bloomberg. Last observation: Feb. 27, 2020.

Smaller effects for 2020 overall and other countries



Source: Bloomberg. Last observation: Feb. 27, 2020.

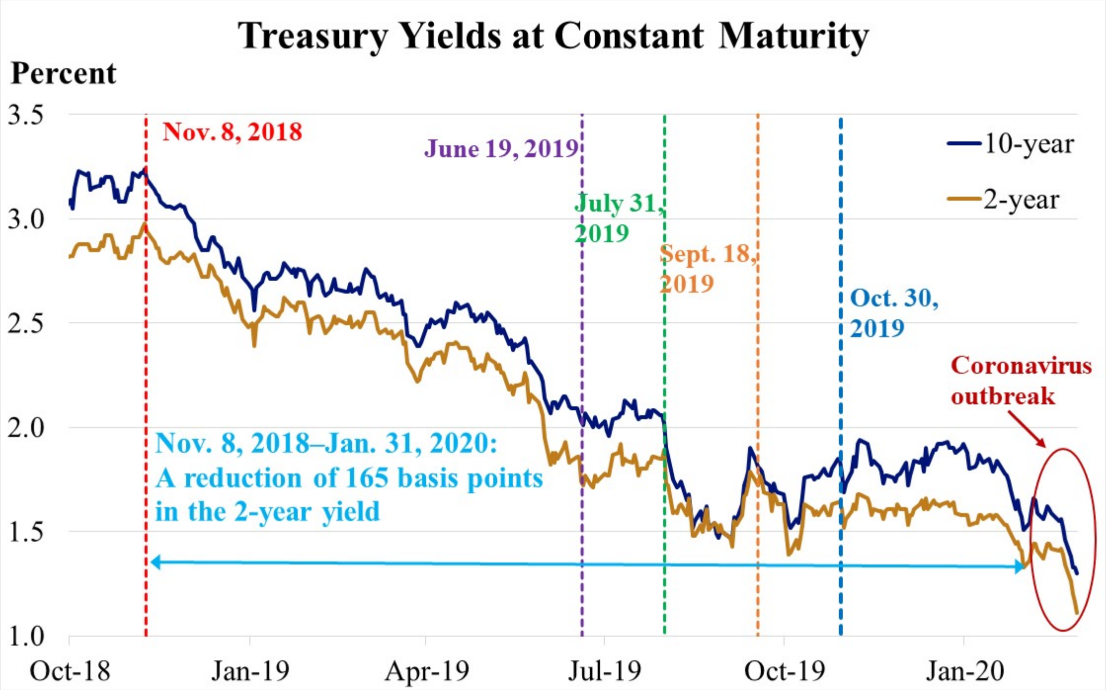
The FOMC Is in a Good Position

Insurance policy rate cuts already in place

- The FOMC executed a marked turnaround in U.S. monetary policy during 2019 that was designed in part to insure the economy against possible negative shocks to growth.
- This has put the FOMC in a good position in early 2020 as we closely monitor the evolving coronavirus impact on the global economy.
- Policy rate decreases have an effect on the U.S. economy with a lag, so last year's rate reductions are likely to continue to have an influence as the coronavirus tragedy unfolds.
- I have argued elsewhere that the adjustment to monetary policy during 2019 was much larger than commonly appreciated.*

** For example, see J. Bullard, "A Sea Change in U.S. Monetary Policy," remarks delivered at the National Economists Club on Aug. 6, 2019.*

Size of the change in monetary policy



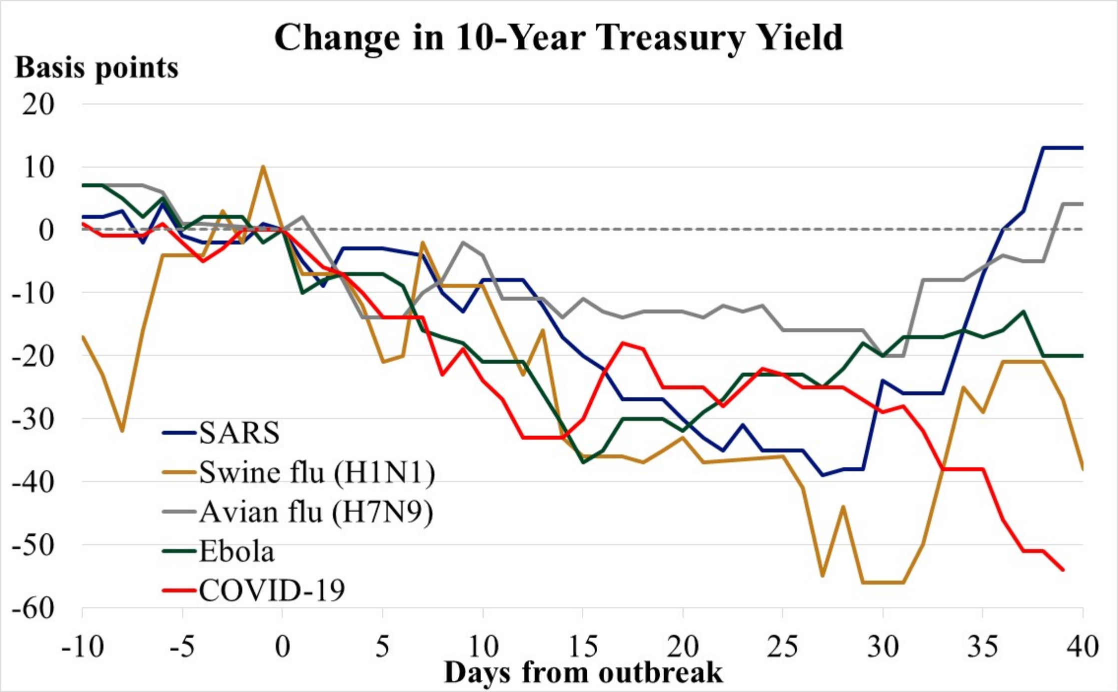
Source: Federal Reserve Board. Last observation: Feb. 27, 2020.

Financial Market Impact

The global flight to safety

- The coronavirus has also been associated with a global flight to safety, pushing longer-term U.S. yields to exceptionally low levels.
- This is a bullish factor for U.S. economic growth above and beyond the declines in yields associated with the 2019 change in direction for U.S. monetary policy.
- Experience with previous viral outbreaks suggests that the effects on U.S. interest rates are tangible and last until the outbreak is clearly contained.

Effect of viral outbreaks on long-term rate

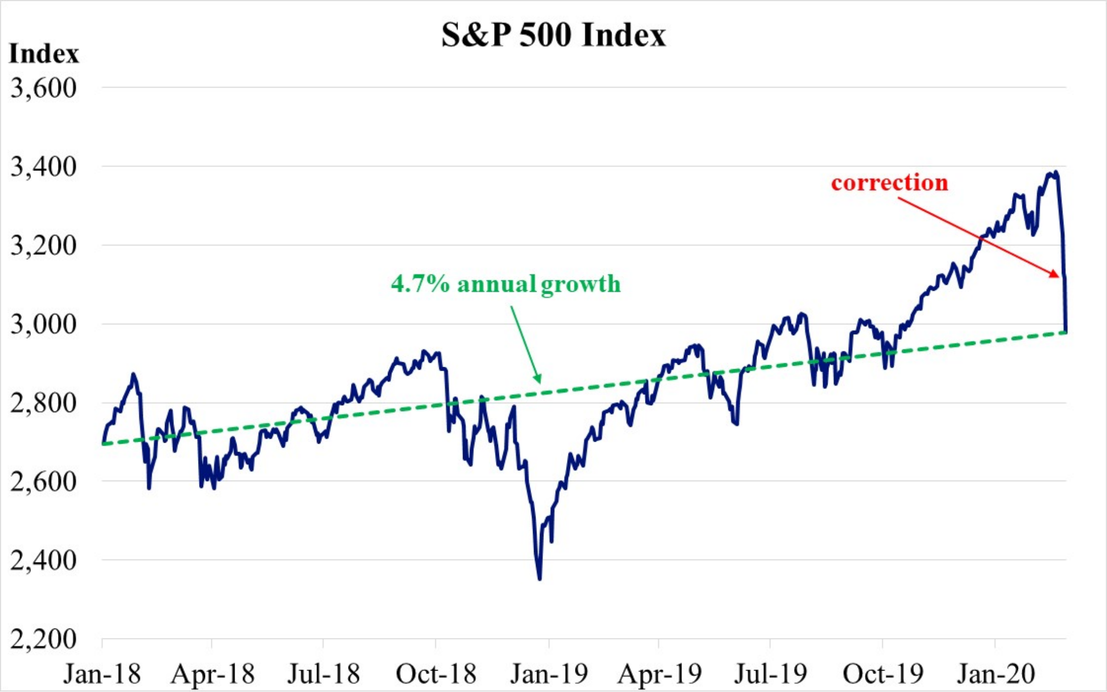


Sources: Federal Reserve Board, Goldman Sachs and author's calculations. Last observation: Feb. 27, 2020.

Equity market impact

- U.S. equity valuations have declined in recent trading due in part to speculation on the impact of the coronavirus on global macroeconomic conditions.
- Some firms' profitability will be directly impacted by the effects of the virus on China and other countries.
- Even with recent equity price declines, the value of the U.S. publicly traded corporate sector has increased at an annual rate of about 4.7% over the last two years.

Stocks extend losses from coronavirus fears



Source: New York Times. Last observation: Feb. 27, 2020.

More Severe Scenarios

The impact in more severe scenarios

- Investors and policymakers are wise to worry about the possibility, still small as of today, that a debilitating global pandemic will develop in the weeks and months ahead.
- This is not what has happened with many other viral outbreaks, but each situation is somewhat different.
- In my view, further policy rate cuts are a possibility if a global pandemic actually develops with health effects approaching the scale of ordinary influenza, but this is not the baseline case at this time.

Fatalities to date compared with influenza

	Deaths	Cases	Mortality rate
COVID-19, China*	2,747	78,630	3.5%
COVID-19, worldwide*	2,804	82,294	3.4%
Seasonal influenza, worldwide**	~291,000-646,000 annually	-	4.0-8.8 per 100,000 individuals

Sources: * *World Health Organization,* COVID-19 Situation Report–38, *Feb. 27, 2020 and author's calculations.*
** *Iuliano, A.D. et al., 2018, "Estimates of global seasonal influenza-associated respiratory mortality: a modelling study,"* The Lancet, *391*(10127), pp. 1285-1300.

Conclusion

Coronavirus in the near term

- COVID-19 is likely to slow global growth temporarily, with much of the slowdown centered in Asia.
- The FOMC is in a good position because of previous policy rate cuts designed to insure the economy against adverse shocks.
- Further policy rate cuts are a possibility if a global pandemic actually develops with health effects approaching the scale of ordinary influenza, but this is not the baseline case at this time.

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