

## Feeling Sick: Markets Take a Black Swan Dive

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SEI recently released its first-quarter Economic Outlook. A summary of the conclusions is provided below:

- The coronavirus (COVID-19) is a black swan that has radically changed the global economic outlook. The U.S. has gone from a full-employment economy to something that can be compared to the devastation wrought by the Great Depression within a matter of weeks. The emergence of the virus has caused financial markets to plunge almost everywhere as the global pandemic spreads rapidly across much of the world.
- The incredible volatility exhibited by both stocks and bonds indicates that investors have had a tough time pricing the uncertainty that has enveloped the global economy. Sharp equity-market corrections exceeding 30% have been recorded in many countries and regions. The onslaught of developments presented by the spread of the virus and a simultaneous collapse in oil prices has forced financial markets to recalibrate prices sharply as expectations about different industries and the overall economy shift at a breakneck pace.
- Sovereign-bond prices have mostly soared, and yields have hit record lows as investors turn to the perceived security of debt issued by national governments. Credit spreads have widened dramatically, however, as investors seek traditionally safer havens like cash and short-term Treasuries. Trading in the bond market has been chaotic, bringing back bad memories of the global financial crisis.
- The ultimate impact on U.S. gross domestic product (GDP) is truly anybody's guess. The first quarter could see a decline at an annual rate of 3% to 5%. The second quarter will likely be one for the record books. Forecasts range from a quarter-to-quarter annualized rate of decline of 12% (estimated by economists at the Bank of America and Credit Suisse) to 30% (estimated by economists at Morgan Stanley). The sudden and widespread stop in economic activity by government is something that has never been experienced on such a scale before. And it came at a time when the U.S. economy, indeed the global economy, appeared to be on an upswing.
- China now seems to be recovering, but the ramp-up is slow. A steep decline in demand for the country's goods in the months immediately ahead, especially from Europe and the U.S., may hold back its rebound. China's internal consumption, however, should rise smartly.
- All central banks are in crisis-fighting mode, having learned valuable lessons during the 2008-to-2009 global financial crisis. While policy rates in the eurozone and Japan remain in negative territory, those of other major economies have been slashed to zero, or are in the process of heading there. Most emerging-market central banks are cutting rates as well.
- Aggressive interest-rate cuts, however, are the least of what central banks are doing to help support their domestic economies. They are dusting off their global financial-crisis handbooks, reestablishing unconventional bond-buying programs and creating some new policies to include more types of collateral that can be accepted in order to extend cash to companies that need it. The Federal Reserve, for example, has committed itself to purchasing unlimited amounts of Treasuries and mortgage-backed securities.
- Nobody knows how much weaker global stock markets will get. It depends on the trajectory of the virus in Europe and the U.S., the robustness of governments' response, and the extent to which the economic shock feeds on itself in terms of corporate financial distress and layoffs.

A full-length paper is available if you wish to learn more about these timely topics.

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