The Coronavirus Hits Stocks

Coronavirus fears took a toll on investors today, with a sharp selloff in European stock markets that spread to the US open. Markets in Germany and France closed down about 4% today, and the US is faring only slightly better. At its lows, the Dow Jones Industrial Average had shed over 1,000 points. The S&P 500 has declined roughly 3% at the time of this writing.

As background, the coronavirus first sickened humans in the Chinese city of Wuhan in late 2019. The virus is believed to have been resident with other mammal species, likely bats, and to have jumped to humans by unknown means. The coronavirus is a genetic relative to earlier SARS and MERS pathogens, although not as deadly. It causes flu-like respiratory symptoms, and is fatal in an estimated 2-3% of infected cases. Following the initial outbreak, Chinese authorities responded aggressively to control further spread of the disease, limiting the movements and activities of tens of millions of citizens, including placing a cordon around Wuhan, a city of eleven million people.

It appears that Chinese efforts to control the spread of coronavirus have met a degree of success, with infection rates dropping inside the country. However, the virus has spread to other countries, having shown up in 28 nations and having infected almost 80,000 people, with numbers certain to climb further.

For the first several weeks of this outbreak, investors registered a collective yawn about coronavirus, believing any interruptions to global growth to be transitory. Today's market selloff seems linked to both "knowns" and "unknowns" that are now worrying these same investors. First, we know that the virus has spread to South Korea and most recently Italy. In each case, infected areas inside the countries are undergoing a familiar routine of monitoring and quarantine, with the knock-on effects of reduced commercial activity affecting a host of industries. In Italy's case, there is added concern that the coronavirus might spread further to populations within the EU, given its open borders and modern roads and rails.

What is unknown is the extent of disruption to the global economy that the coronavirus will cause. A small but growing number of companies—including Apple—have disclosed that they are certain the coronavirus will impact their quarter and possibly more, although they are unable to quantify the effect. While it is a given that travel-linked companies including airlines, cruise lines, and hotels will suffer a near-term impact from the virus, we will soon be learning the impact from delays and disruptions to *supply chains* across a host of industries. China supplies raw material and early-stage production inputs for a host of key industries, including pharmaceuticals, electronics, autos, and other complex manufacturing. Large swaths of the country were idled in January and February, and the country is by no means back to normal throttle.

At this juncture, our view is that the coronavirus outbreak will be contained, but not without some short-term hit to growth. Fortunately, our domestic economy remains on firm footing, led by the household sector and a buoyed by a strong jobs market. It is increasingly likely that the Fed will institute one or more additional rate cuts in coming months, which would be investor-friendly moves.

We continue to monitor coronavirus developments closely. A fair bet is for continued investor concerns and market chop, especially in response to perceived bad news. At the same time, when the first indications arrive that the tide is turning against the infection, the prospects for a significant relief rally are, in our estimation, quite favorable. It is ironic that our modern methods to track, report, and contain a disease outbreak no doubt contribute to heightened anxieties from the very populations this information is intended to benefit. In an earlier age, coronavirus might have been mistaken as a bad strain of the flu and we would have been none the wiser.