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Our views

Although there are near-term downside risks to China’s economic growth, Asia/EM corporate earnings and global equity market performance, we see scope for a recovery once the growth rate in 2019-nCoV cases starts to decline. Overall, we remain overweight global equities and maintain a pro-risk stance in our multi-asset portfolios

Global markets in risk-off mode amid rise of new virus

Global equity markets have sold off over the past week or so amid concerns regarding the spread of the novel coronavirus (2019-nCoV) (Figure 1). This new strain of coronavirus follows similar outbreaks in 2002 (Severe acute respiratory syndrome, SARS-CoV) and 2012 (Middle East respiratory syndrome, MERS-CoV). The reproduction rate of 2019-nCoV is currently higher than that for SARS, but the mortality rate is significantly lower at around 2% versus 10% for SARS.

Authorities in China have taken unprecedented measures to contain the outbreak, including placing a number of cities under shutdown, while extending the Lunar New Year holidays by three days until 2 February. Authorities in Hong Kong have restricted transport links to China.

What will the economic impact be?

The disruption associated with attempts to contain the spread of the virus, combined with confidence effects, is likely to weigh on near-term growth in China. By way of comparison, the experience of SARS which broke out in late 2002 saw China’s GDP growth rate fall from 2.9% qoq in 2003 Q1 to 0.9% in Q2 amid a large decline in retail sales growth (Figure 2), and a sharp hit to tourism activity.

However, the impact was short lived with a rapid rebound seen in the second half of 2003. Full-year GDP growth in 2003 was 10%, versus 9.1% in 2002.

A V-shaped recovery therefore seems like a reasonable baseline assumption at present. However, uncertainty around how quickly the virus can be contained makes estimating the exact magnitude and duration of the expected downturn difficult to forecast. Two further factors should also be taken into account:

- China’s economy has developed significantly since 2003, and now has a lower trend growth rate and is more dependent on domestic demand than exports. Nevertheless, a large shift to online shopping can help retail activity (assuming deliveries are not significantly impeded).
- China now accounts for close to 20% of global GDP (adjusting for price differences), more than double its 2003 share, so a modest, short-term spillover to global growth can be expected. Asia/Emerging Markets/commodity exporters are likely to be most exposed.

What next for markets?

There has been less of a drawdown in equities during the 2019-nCoV episode so far versus SARS at the same stage of outbreak, although global risk assets may remain under pressure in the coming weeks as cases continue to rise.

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Market considerations

Although there are some near-term downside risks to China’s economic growth, Asia/EM corporate earnings and global equity market performance, we see scope for a recovery once the growth rate of 2019-nCoV cases starts to decline. Also, as we saw in 2019, policymakers can support economic conditions if needed (with room for both monetary and fiscal policy easing in China). Overall, we remain overweight global equities and maintain a pro-risk stance in our multi-asset portfolios.
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