16 March 2020

What to do in a Crisis?

Where do we start with recent events! In the past week, the World Health Organisation (WHO) has declared COVID-19 a pandemic; major events, schools and public gatherings have been shutdown around the world and travel bans have taken place.

The reaction in financial markets has been tumultuous. Some of the daily falls in equity indices towards the end of last week were the largest since the October crash in 1987. Around the world, one-by-one, central banks have stepped in to provide measures in an attempt to bring some sense of calm. Last week, central banks in the UK, Europe, China and Canada have cut their policy rates, or expanded their monetary easing. This morning, the Reserve Bank of New Zealand (RBNZ) and the US Federal Reserve joined ranks and slashed their official policy rates in emergency meetings, to 0.25%, and 0-0.25%, respectively. The Bank of Japan is expected to announce a decision from an emergency meeting today.

This morning, the RBA released an announcement, implying that it too, will announce additional policy measures on Thursday. We suspect that these measures will include a 25 basis point rate cut, taking the cash rate to 0.25%. Additionally, the RBA stated today that it “stands ready to purchase Australian government bonds in the secondary market…” implying that some form of quantitative easing program could also be adopted.

Governments are also trying to mitigate the blow to economic growth with fiscal stimulus being deployed, including a $17.6 billion stimulus package from the Australian government announced last week.

The potential blow to economic activity is hard to fathom, and unprecedented in recent times. But no matter what authorities throw in terms of providing stimulus, a major hit to the economy would seem unavoidable. Self-isolation, travel restrictions, cancelling of events and caution by the public are also what may be necessary to prevent a wider spread of the virus. Fiscal and monetary policy stimulus can only soften the blow. We do not think that Australia can avoid a technical recession over 1H2020, and it seems likely that the unemployment rate will rise.

We will await Thursday when the RBA is scheduled to make its announcement. Thursday will also see the release of Labour Force data. While we expect that labour market conditions will deteriorate in coming months, the negative impact to the labour market in February is expected to be limited to hours worked. We expect a modest 7k increase, and for the unemployment rate to remain steady at 5.3%. The bulk of job declines may not occur until data for March is released.

The minutes of the RBA meeting in March will be released tomorrow, but these will be irrelevant after the rapid turn of events since that meeting was held.

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Forecasts

Due to the rapid change of recent, current and future developments, we have decided to not publish our forecasts this week. Please contact us if you would like further information or elaboration of our views.

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