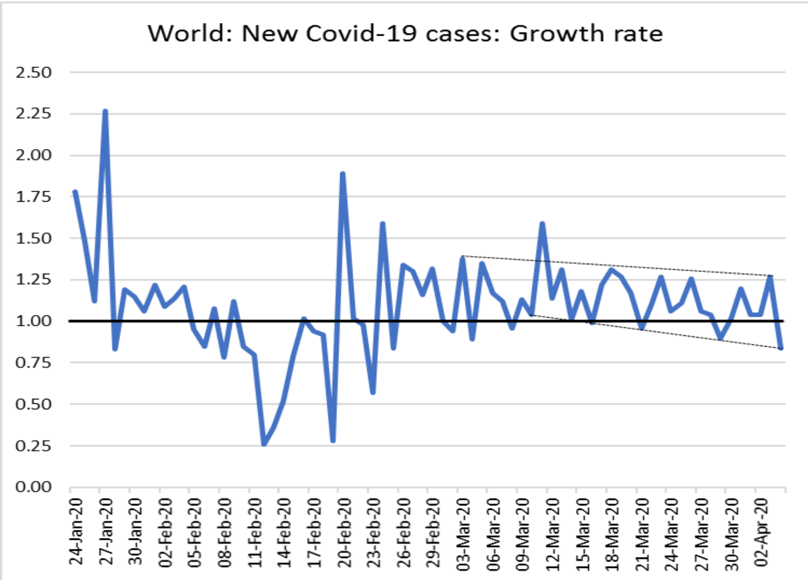
THE COVID-19 DISEASE AND ITS IMPACT ON THE ECONOMY AND FINANCIAL MARKETS

The fear caused by the spreading and mortality rates of the Covid-19 disease wreaked havoc on financial markets – until governments and central banks intervened. That halted the free fall and contributed to some recovery in the prices of shares and bonds worldwide. Central banks reduced interest rates and made sure enough liquidity is available, while governments and private sector companies provided assistance packages to companies and households in distress. But for markets to recover further, "a fast decline in the spreading of the virus" is needed.

The key to the end of the crisis is in a vaccine. But, in its absence, the alternative is measures to reduce the rate at which the virus is spreading. In this respect, social distancing and lockdowns are implemented around the world. Its success will be determined by the growth rate of new cases – that is when new cases the next day is lower than the current day. A number lower than 1 (declining fast to 0) is what is needed for these approaches to be successful. The growth rates are increasing in some countries (e.g. USA) and declining in others. Although the rolling weekly average for the world is still more than 1, the good news, as the graph below shows, is that the daily world growth rate is declining – as "lower high" and "lower low" growth rates are registered. But, it is happening very slow – the next two weeks will be crucial for success. If successful, lockdowns in some countries may be replaced by strict social distancing measures. If not, lockdowns may continue for longer.



In South Africa, the weekly moving average growth rate declined from 1.32 on the day of the lockdown (26 March) to 1.05 on 4 April. The same numbers for the world are 1.13 - and also 1.05. At this early stage it seems as if South Africa's measures are working – but as the growth rate is still more than 1, chances are slim for the lockdown to end on 16 April.

This indicator should also signal the outlook for the resumption of economic activity, as well as market movements. The faster the decline, the higher the hopes for a resumption of economic activities – and vice versa. Due to uncertainty, it is difficult to make economic forecasts. However, several institutions attempted this exercise. For instance, JP Morgan worked on the assumption that the pandemic ends by end June. If so, a two-quarter GDP contraction is expected in the USA (-10% in Q1 and -25% in Q2) and the Euro Area (-15% and -22%). Thereafter, economic growth is expected to increase by 6% over the final two quarters in the USA (assuming that social distancing policies are significantly relaxed by mid-year.) China's Q1 growth may experience a huge decline of 41% but can register a V-shaped recovery, rebounding by 57% in the second quarter. China's full-year GDP growth forecast is 1.1% (from an initial 5.9%). The world is expected to register growth of around 0.3% in 2020, increasing to 3% in 2021.

In South Africa, the best-case scenario is for the economy to shrink by 2% in 2020, but It can be 4-6% in worse cases. South Africa's woes were aggravated by the inevitable decision of Moody's on 25 March to downgrade the country to junk status with a negative outlook. And the economy will be confronted by huge job losses amid electricity shortages. Under these circumstances, the South African Reserve Bank will have little choice but to reduce the repo rate further. Markets, on the other hand, recover before economic indicators. If things work according to plan (growth factor declines fast), the partial recovery over the past two weeks may continue. For instance, at its lowest point the JSE ALSI was down 34.9% since the start of the year, but recovered to end the month 22.1% down. Similarly, the All Bond Index was 16.6% down, but improved to be 8.7% down by end March. However, continued volatility in the markets will persist – as international and domestic economic indicators emerge to indicate the magnitude of the virus' impact. This, the growth rate of the spreading and other government measures will impact markets going forward.

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