Focus

Feature Article

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A Bridge Over Troubled Markets

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After another tumultuous week for markets, conditions finally showed some semblance of stability in the final days. A wave of policy measures helped smooth out some of the rougher edges in market disruptions, and raised confidence that the economy can recover later this year. Despite the late-week improvement in tone and market functioning, stocks still took another big step back (the S&P 500 fell about 12%), the US$ ended significantly higher, and oil sunk a further 30% (even with a massive pop on Thursday). Bonds also had another wild ride, even Treasuries—the 10-year yield saw a swing of roughly 60 bps in three days, yet finished the week little changed at around 1%. But in a clear sign that the tidal wave of liquidity is working, both equity and bond prices rose on Friday morning—last week had witnessed the troubling reverse move (i.e., both stock and bond prices falling).

While it may be too early to call a bottom, a somewhat more normal-functioning market at the least suggests the most dramatic swings are past. **And now, we await the hit to the economy.** This week also saw widening shutdowns, even digging into the retail and auto manufacturing spaces, and a surge in layoff announcements. Of course, that ramping up of misery was met by much more aggressive policy responses. **First, the Fed didn't even wait for its Wednesday FOMC meeting and unleashed a three-pronged set of measures on Sunday** (yes, it's been less than a week!), most notably a 100 bp slash in rates to the financial crisis low of 0-to-0.25%, and $700 billion in QE4. **Next, Washington got busy on the fiscal front**, first passing support for unemployed workers, then getting close to an over $1 trillion stimulus package (more than 5% of GDP), including direct cheques to Americans.

The key question is whether this massive stimulus package—and it is at least comparable to the steps taken in early 2009—is enough. It's not enough to avert a massive decline in economic activity in the spring months; there's almost nothing that would be enough to offset that, given the mandated shutdowns and closures, including the State of California. Next Thursday's initial jobless claims report is almost certain to deliver a jolt of reality, with a staggering rise in the past week alone. But we believe **the fiscal steps are enough to help propel the economy into a forceful recovery in the second half of the year**.

The U.S. is not alone on the fiscal side, with **all of the G7 economies unveiling stimulus, or preparing to do so**, even Germany. While most are looking at something more modest as a share of GDP than the U.S. measures, the steps are still significant. Canada is actually fairly typical on that front, with **Ottawa announcing $27 billion** (or 1.2% of GDP) **in direct new spending** this week, with most aimed at the most vulnerable workers. As well, Finance gave a four-month delay to those owing taxes, a significant measure that will provide some breathing space. In general, most of the policy changes are structured to bridge the gap for workers and the economy over the shutdowns. Finance Minister Morneau was quite clear that **this won't be the last word** on fiscal steps, and reports indicated that a support package for the battered energy sector is coming next week. Even so, the Canadian dollar was clocked, along with many other currencies, sliding more than 3% to below 70 cents, further skewered by the slide in WCS to a record low below $10/bbl at one stage.

Now let's turn to what this week's series of events means for the economy. For full disclosure, **these estimates are based on an assumption that the widespread shutdowns last roughly two months, or to around the middle of May**. At that time, we see activity beginning to bounce back as the closures lighten; then, conditions gradually get back to something closer to normal over the summer months. We certainly do not view this as overly pessimistic, and may even still be optimistic, but it is encouraging to see that new cases in China have essentially ground to a stop.

On what this implies for the data, we would repeat what we said last week: Events are unfolding much more rapidly and intensely than we had previously expected, bringing the economic weakness forward, so we are **adjusting our forecasts for 2020 yet again this week**. The closure of the U.S./Canada border to all but essential travel is just an example of how extreme this episode has become. In summary:

- **Global growth** is now expected to be just 0.8% this year (from 1.6%), a deep slowdown from last year's sluggish 2.8%, and by far the weakest year since 2009. We took a heavier axe to Europe, China, North America and emerging markets—i.e., everyone. Partly as a result, we have further cut into the oil price forecast, and now look for an average of $35 for WTI this year (versus $40).

- **U.S. GDP** is now expected to contract moderately in Q1, and then fall at a 10% annual rate in Q2. We continue to expect a strong rebound in H2, but the entire year will likely see a 0.5% drop, versus an estimate of a small 0.5% gain previously (which was already a big step down from 2.3% in 2019). While the double-digit drop in Q2 GDP may look extreme, we would note that some other forecasters are even more negative. A deeper near-term drop is certainly possible, but the fast wave of fiscal stimulus could help limit the spring drop. Inflation has been chopped further by the slide in oil.

- **Canada's GDP growth** is being cut to -1.0% this year, down a full point from last week's call of zero (and versus a 1.6% rise for all of last year). Canada will likely take an even heavier hit due to the slump in commodity prices (especially oil), and also a lighter boost from fiscal stimulus, at least up to this point. Here, too, we expect a big Q2 contraction (down 10%) after a 2.5% drop in Q1, but also a big rebound in H2. We had previously looked for no growth in Q1, but the sudden and widespread closures this week obviously mean that March will be much weaker than earlier expected.

- **The outlook for interest rates is much more straightforward now, especially for the Federal Reserve.** With rates now essentially at zero, we don't expect any further moves on the U.S. rate front right out to the end of 2021 (i.e., also no negative rates). **The Bank of Canada** is a tad more interesting, with Governor Poloz giving a pass on a prime-time opportunity this week to cut again after last Friday's 50 bp chop. We still look for another 50 bp cut down to the crisis low of 0.25%, but it may well not happen until the mid-April meeting.

- **The Canadian dollar** buckled heavily this week, in part due to a broad surge in the U.S. dollar and, in part, due to desperately low oil prices. We see the currency remaining under pressure in the months ahead, with a possible test of the $1.50 level (or below 67 cents). We look for the loonie to settle down along with other markets by the second half, but it will be challenged to get back above the 75-cent level even in 2021.

It's now patently obvious that we can't make any guarantees on the life-span of these forecasts, and we will take it on a week-by-week basis. Consider that it was precisely one month ago today that the TSX hit a record high (one day after the U.S. major averages), and clearly the world has changed massively in that short span. Investors, analysts, and economists are all grappling with this dramatic change but, like markets, it seems that forecasts are iterating to the new reality.

The sudden onset of this crisis is a key feature; it's almost as if every crisis the market has faced in the past 25 years have been collapsed into one single event in quadruple time. There have been features of **the 2008/09 crisis**, with market dislocations and the Fed wheeling out an alphabet soup of measures and zero rates. We've had echoes of **the 2014-16 oil shock**, with record lows on WCS to boot. There are tremors similar to **the 2009-12 euro crisis**, with Italian spreads surging this week, and the ECB rushing in with aggressive QE. And, there are similarities with **9/11**, notably the sudden stop in travel, and talk of bailouts for airlines. The incredibly swift fall in stocks even conjures memories of the **1987 crash**. And, all of this is unfolding at a time when most of us are working at home, and discovering the telecommunications constraints—one estimate suggested internet traffic surged 30% this week. Ending upbeat: note the absence of the word COVID-19 in the commentary above.

U.S. Policy: It's All about the Acronyms... and the Benjamins

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The actual and prospective economic and credit market consequences of the escalating COVID-19 crisis is eliciting a similarly swift swelling of monetary and fiscal policy responses. After a record reduction in policy rates this month—the two moves totalling 150 basis points is the most in any single month since the FOMC began targeting fed funds in the 1980s—the Fed has been dusting off the alphabet soup of liquidity facilities from the time of the Global Financial Crisis... the "Acronyms". Meanwhile, the Administration and Congress are working on a third, potentially $1 trillion-plus, fiscal package to help cushion the coronavirus blow... the "Benjamins" (in case you're not a hip-hop music fan, the reference is to the face on the $100 bill).

On March 17 and 18, in a span of less than 37 hours, **the Fed announced the establishment of a Commercial Paper Funding Facility (CPFF), Primary Dealer Credit Facility (PDCF), and Money Market Mutual Fund Liquidity Facility (MMLF)**. The CPFF is a special purpose vehicle set up to purchase unsecured and asset-backed commercial paper directly from eligible companies. The PDCF is, in effect, a "discount window" for primary dealers, but with different eligible collateral than the traditional discount window for banks (e.g., equities can be pledged). The MMLF will make loans to eligible financial institutions to fund their purchases of high-quality assets from money market mutual funds.

These liquidity facilities, along with the overt encouragement by the Fed and other federal regulators for banks to use the discount window along with their capital and liquidity buffers, are designed to support the flow of credit to businesses and households at time when a significant crimping of credit flow could exacerbate an already severe economic downturn.

As most parts of the economy have slowed and some parts have shut down completely, businesses, both large and small alike, have seen their cash flows slow significantly or dry up altogether. For some firms (and individuals), with existing lines of credit at banks, and other firms, with credit lines and commercial paper programs, these sources of liquidity are being tapped… in some cases to their full extents. As credit lines are drawn down, liquidity in the banking system is reduced at the same time that lenders are likely becoming more leery about increasing loans amid heightened economic uncertainty. Meanwhile, commercial paper investors, either directly or indirectly via mutual funds, are also becoming more concerned about getting their capital back, causing some sales/redemptions or less buying than before. This week, evidence that liquidity and money market pressures were becoming problematic was provided by the spike in CP rates and the fact that the fed funds rate was trading at the top of its new 0%-to-0.25% range.

On the federal fiscal front, it began with a trickle. On March 6, the President signed the **Coronavirus Preparedness and Response Supplemental Appropriations Act**, worth $8.3 billion. It mostly supports the public health system. The tap opened a little more when the President signed the **Families First Coronavirus Response Act** on March 18, worth more than $100 billion. It mostly supports laid off workers or those on sick leave, along with food assistance for children no longer in school and, for some, free COVID-19 testing. Now the Administration and Congress are working on a spending bill that could easily top $1 trillion. The largest part of this package is made up of direct payments to individuals and families, along with funding for small business loans. Some lawmakers (mostly Democrats) are balking at loans for industries such as the airlines, and argue that still not enough is being directed to public health. Any Senate version needs 60 votes, thus bipartisan support, to move on to the House. It's looking like this bill might only land on the President's desk next week.

And, we judge this won't be the last time policymakers will feel compelled to act. As Sal notes below, **the economy is going to look awful for the next month or three** (at least), and we doubt elected officials—in an election year—will want to be seen sitting on their hands.

U.S. Economy: Q2 Contraction Will be Nasty

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Amid the latest wave of closings, cancellations, and layoffs of the past week, there's little doubt now that the U.S. economy is headed for a steep downturn. The only question is how severe and long it will last. For the most part, that will depend on how effective social distancing is in flattening the outbreak curve. No one has a good answer, though recent successes in China, South Korea, Singapore and Taiwan in slowing the outbreak offer some hope. Until then, we can only provide a rough estimate of the economic dislocations to come. What we do know is that activity is coming to a screeching halt across much of the nation. California has ordered its citizens to stay home except for essential activities. The major automakers have closed plants at least until month's end. And, millions of retailers and other businesses have now shuttered their doors for safety reasons and absence of customers.

The early data for March (some documented in the Feature) only hint at the punishing toll of the virus on the economy. Both the Empire and Philly Fed manufacturing indexes posted their single-largest monthly declines on record. A 70,000 spike in jobless claims last week, the third biggest in the current century, captured the first wave of massive layoffs that are surely to eclipse the 665,000 reached in 2009.

Ohio alone reported more than 139,000 new claims in the first five days of the current week. Although some businesses are beefing up staff to handle a surge in essential needs, including grocery and drug stores, online shops, and health care, others in the travel, hotel and restaurant industries have already announced millions of layoffs.

We have sliced our first-half GDP forecast further, taking Q1 down to -2.0% annualized and chopping Q2 to -10%. The latter is worse than the -8.4% registered at the worst point of the Great Recession, and it could be much deeper. For now, we can only assume that activity slowly begins to return by mid-May after a virtual two-month shutdown for many businesses. In this case, GDP could snap back with purpose in the second half of the year due to pent-up demand and the massive policy rescue effort underway. Still, growth will be negative in 2020 (-0.5%), before returning to a healthier 2.5% rate in 2021. Meantime, the jobless rate looks to kick up from 3.5% currently to above 5% in the months ahead, before settling back to 4.5% by year-end. Core PCE inflation will likely sink toward 1% from the current 1.6%.

Much will need to go right in the weeks ahead for even this dour projection to pan out. But if everyone practices social distancing (the cause of the recession but also the cure for the pandemic in the absence of a vaccine), and many stakeholders practice forbearance to prevent a wave of individual and business bankruptcies, and policymakers keep tackling the pandemic (finally) with gusto, we will at least stand a reasonable chance of avoiding the five quarters of economic contraction experienced in the Great Recession.

Bank of Canada Focused on Liquidity… For Now

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After a wild two weeks of central bank manoeuvres, the Bank of Canada is once again left with the highest policy rate in the developed world after holding the line this week. The BoC cut rates 50 bps last Friday to 0.75%, but resisted the temptation to ease again despite a huge move by the Fed to start the week, a massive QE expansion by the ECB, another rate cut and QE by the BoE, a rate cut and QE from the RBA, etc.

What exactly is the BoC waiting for? Accompanying FM Morneau during the release of the federal fiscal stimulus measures, Governor Poloz appeared to be very patient, noting that he's waiting for fresh forecasts at the moment. Newsflash, the outlook has deteriorated massively! We've downgraded our forecast once or twice a week since the start of the month, and there's little chance we're done. That being said, the world is not ending and the economy will get through this, and when we do, the rate cuts can be reversed if the BoC is still concerned about financial vulnerabilities.

For now, **the Bank appears to be focused on liquidity measures** and there have been plenty introduced over the past two weeks. Here's a brief summary:

- Bi-weekly 6-month and 12-month term repo operations
- Broad expansion of collateral eligibility
- Bankers' Acceptance Purchase Facility (starts next week)
- Purchasing Canadian Mortgage Bonds (CMBs) on the secondary market (up to $500 mln per week)
- Increased number of GoC buyback/switch operations
- Launched Standing Term Liquidity Facility (effective March 30)

Once all these measures have been rolled out, they will support liquidity in financial markets, but broader tension remains due to the economic backdrop and risk environment.

Another reason the BoC might have held its fire on another 50 bps in cuts is due to the **sharp decline in the Canadian dollar**. While the plunge in oil prices suggests the loonie should be weaker, the pace of the drop has been staggering. Recall that in January 2016, a sharp drop in the C$ prompted Governor Poloz to hold rates steady despite expectations of a cut. The currency has been better behaved the past couple of days, and if this continues into next week, perhaps that's enough to prompt the Bank to pull the trigger.

Key Takeaway: While the BoC has the highest policy rates in the developed world, that's likely to change within days, if not weeks. The liquidity measures introduced over the past two weeks will help markets, but the extraordinary drop in economic activity that's underway will prompt another 50 bp rate cut and potentially QE from the Bank of Canada.

Central Banks... "Clear your calendars and jump on the call!"

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Central bankers completely trashed plans for regularly scheduled monetary policy meetings this month. The speed at which the COVID-19 virus was spreading was bringing global growth and financial markets to their knees. Tough decisions needed to be made and they could not wait for the next meeting. The Federal Reserve kicked it off with its emergency inter-bank announcement on March 3rd. Then, essentially, other banks followed suit. Here are a few...

Bank of Japan: The BoJ has not met outside of its scheduled time since November 2011. But this week, it couldn't wait until Thursday. After an emergency meeting on Monday, Governor Kuroda announced that the Bank would leave rates as is (policy balance rate at -0.1%, aim for ~0% on the 10-year JGB), but it would bump up its asset purchases (ETFs, corporate bonds and commercial paper) and set up a new lending facility to extend credit for companies hit hard by the virus. And, the Committee promised that it "*will not hesitate to take additional easing measures if necessary.*"

European Central Bank: Perhaps in an effort to show that it is not asleep at the wheel, the ECB held an emergency meeting on Wednesday evening and, shortly after, announced that it was launching the all-new €750 bln Pandemic Emergency Purchase Program, or PEPP for short. Much like the other envelope that was announced on March 12 (€120 bln), this is temporary in nature, and will terminate once the Governing Council judges that the coronavirus is over. But the central bank is assuming the funds will be in use until the end of the year. So that brings total bond purchases this year to €1.1 trln (including the other €20 bln per month purchase). Key lending rates were unchanged, though. In the words of President Lagarde, "*...there are no limits to our commitment to the euro.*"

Bank of England: The BoE also surprised us with its second cut in two weeks. On March 11, under then-Governor Carney, the MPC slashed Bank Rate 50 bps to 0.25%, cut the countercyclical capital buffer rate to 0% and launched a Term Funding Scheme for Small and Medium Firms (aka TFSEM). On March 17, guided by newly-installed Governor Bailey, the Bank launched a COVID Corporate Finance Facility (or CCFF), allowing it to buy an unlimited amount of commercial paper. Then, the BoE, too, held a special meeting on March 19, and announced that a 15 bp cut to Bank Rate to 0.10%, an increase in the Asset Purchase Facility by £200 bln to £645 bln, and a boost to the TFSME. As Governor Bailey declared, "*we needed to act now*"; they could not wait to have the economic data in hand.

Reserve Bank of Australia: The RBA already lowered the cash rate 25 bps to 0.50% on March 3rd. Alas, it couldn't wait until the next meeting on April 7th; instead, it held an emergency meeting on March 19, trimmed the cash rate again by 25 bps to 0.25%, and entered the world of QE. It took a page from the BoJ's playbook by targeting a 0.25% yield on 3-year AGBs (the BoJ targets 10-year JGBs at around 0%); and, it planned to purchase state government bonds. It also took a page from the BoE's playbook and launched a 3-year term funding facility to help smaller businesses. Governor Lowe expects the hit to the economy to be temporary but in the meantime, the virus was causing a "*major economic problem and it's having deep ramifications for financial systems right around the world.*"

Reserve Bank of New Zealand: Neighbouring New Zealand also eased this week. The next planned meeting date was April 14th and that was light years away. So, the RBNZ held an emergency meeting on Sunday and slashed the Official Cash Rate 75 bps to 0.25%, where it will stay for at least a year. If more stimulus is needed, the central bank said it "*a large scale asset purchase programme of NZ government bonds would be preferable to further OCR reductions.*"

There were many other central bank moves this week (except for the PBoC, which held steady). But it is clear that monetary policy can only go so far; fiscal stimulus is needed. And it has begun as we have seen in Italy, the U.K., Australia and New Zealand. Germany is mulling over various plans, including a €180 bln direct support programme. And, Eurozone finance ministers are looking at the €410 bln ESM. So it is finally happening. **If there is ever a time for governments to step up, this is it.**

Canadian Governments: Spend Now, Count Later

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Canada's budget season has been thrown into disarray by the COVID-19 outbreak. At the federal and provincial levels, **governments have next to no visibility** on the revenue line due to an expected dramatic falloff in economic activity, and will see spending pressured sharply by health care demands and stimulus/support measures. At this point, it looks like governments across Canada are going to focus all of their energy on the latter, and only worry about the bottom line later on when the dust settles.

The **federal government** this week announced a range of short-term measures to support the economy in the months ahead, rolling out $27 billion worth of direct support. That's substantial (just under 1.2% of GDP) and, importantly, relatively quick (most dollars will be flowing in April or early-May). For some perspective, the deficit for the coming fiscal year was last estimated at $28 billion. Add this week's measures, plus more to come, and a deep deterioration in the underlying economy, and a shortfall approaching triple digits could be coming.

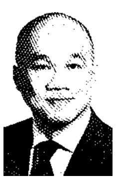
Meantime, the provincial budgets that have been tabled were already out of date when they rolled off the printer. For example, **Alberta's** FY20/21 document ($6.8

billion deficit) was based on stiff fiscal restraint *and* $58 WTI, versus recent levels below $30. With a reported $3 billion stimulus package in the works (if not more), the deficit could easy blow through $15 billion this fiscal year, or 4% of GDP. That would top levels seen during the 2015/16 oil shock, and be outsized only by those during the mid-1980s. Hence the DBRS downgrade this week, and negative rating outlooks on the other oil producers.

Elsewhere, **Ontario** will roll out a short fiscal update next week as a venue to deliver a package of stimulus measures. Rightfully, they probably believe that a full budget exercise is pointless at this time. This week's **Manitoba** budget was a great example of this. While the Province published a full fiscal outlook, they were clear in their admission that those figures won't hold. To account for that, the Province laid out a matrix of potential budget impacts, based on varying degrees of stress on health spending and economic performance. For example, in a case where both the economic (0.5% GDP hit) and health spending impacts are modest, the $220 million deficit would worsen by $110 million. At the other end of the spectrum, a 2.4% reduction in real GDP growth and a 'high' impact on health spending would carve $682 million from the bottom line.

The Bottom Line: Canadian governments are aware that their budget balances are in for a world of hurt. At this point, most are making the decision to do what is necessary from a stimulus/support perspective, and worry about the bottom line at a later date.

Emerging Markets: In the Line of Fire



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Although many of the world's largest emerging markets (EMs) have reported only a small number of confirmed COVID-19 cases so far, their stock markets and currencies have been hit hard. Moreover, it appears that **many EMs are at risk of facing a prolonged 'sudden stop' in external financing**, particularly U.S. dollar funding, as global investors are indiscriminately reining in capital in response to deteriorating global economic conditions and a strong desire to batten down the hatches. This probably explains why even the emerging world's most liquid currencies (Brazilian real, Mexican peso and South African rand) are witnessing the highest pace of capital outflows. The movements in these currencies likely reflect a multitude of global economic trends and risks, the health of China's economy (Brazil), world demand for hard commodities (South Africa) and general EM risk (Mexico). The pressures would intensify if an EM was forced to shut down its economy to contain a large COVID-19 outbreak.

In an effort to help contain the pressures, **the U.S. Federal Reserve** announced yesterday that it had **re-opened swap lines** with nine additional central banks, including Brazil and Mexico. The other central banks given access were Australia, Denmark, New Zealand, Norway, Singapore, Sweden and South Korea. Note the Fed has permanent swap arrangements with the central banks of Canada, the ECB, Japan and Switzerland. This is good news for these central banks and their respective banking systems as it acts as a powerful signalling device and gives them additional access to U.S. dollars when in need. On the flip side, other large EMs that do not have the Fed's swap line (e.g., South Africa and Turkey) could face greater pressures.

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Indications of stronger growth and a move toward price stability are ***good news*** *for the economy.*

Canada

- Ottawa pledges $27 bln in COVID-19 fight
- WTI plunges to near $20, WCS touches single digits before climbing
- C$ drops below 70 cents

Good News

Manufacturing New Orders +0.8% (Jan.)

Existing Home Sales +5.9% (Feb.)

MLS Home Prices +5.9% y/y (Feb.)

New Housing Prices +0.6% y/y (Feb.)

Consumer Prices +2.2% y/y (Feb.)

Global investors bought a net $17.0 bln of Canadian securities (Jan.)

Bad News

Retail Sales Volumes -0.3% (Jan.)

Manufacturing Sales Volumes -0.4% (Jan.)

United States

- Fed cuts 100 bps to near zero; announces asset purchases totalling $700 bln
- Pres. Trump pushes for over-$1 trln fiscal relief package

Good News

Industrial Production +0.6% (Feb.)—and **Capacity Utilization** +0.4 ppts to 77.0%

Existing Home Sales +6.5% to 5.77 mln a.r. (Feb.)

Global Investors bought a net $28.0 bln of U.S. securities (Jan.)

Job Openings climbed to 6,963k (Jan.)

Current Account Deficit narrowed to $109.8 bln (Q4)

Leading Index +0.1% (Feb.)

Bad News

Retail Sales -0.5% (Feb.)

Initial Claims +70k to 281k (Mar. 14 week)

Housing Starts -1.5% to 1.599 mln a.r. (Feb.)

Building Permits -5.5% to 1.464 mln a.r. (Feb.)

Empire State Manufacturing Survey -7.4 to 49.5; **Philly Fed Index** -10.9 pts to 47.1 (Mar.)—both on an ISM-basis

Business Inventories -0.1% (Jan. F)

NAHB Housing Market Index -2 pts to 72 (Mar.)

Japan

- BoJ ups ETF purchases; announces bank lending program

Good News

Core Machine Orders +2.9% (Jan.)

Industrial Production revised up to +1.0% (Jan.)

All-Industry Activity Index +0.8% (Jan.)

Bad News

Exports -1.0% y/y; **Imports** -14.0% y/y (Feb.)

Consumer Prices slowed to +0.4% y/y (Feb.)

Europe

- ECB unleashes €750 bln bond purchase program
- BoE cuts 15 bps to 0.1% in emergency move and increases bond purchases
- Norges Bank slashes 75 bps to 0.25%

Good News

Italy—Industrial Orders +1.2% (Jan.)

U.K.—Employment +184,000 (3 mths to Jan.)

Bad News

Euro Area—Trade Surplus narrowed to €17.3 bln (Jan.)

Germany—ZEW Survey -58.2 pts to -43.1 (Mar.)

Germany—ifo Business Climate -8.3 pts to 87.7 (Mar. P)

U.K.—Jobless Rate +0.1 ppts to 3.9% (3 mths to Jan.)

U.K.—Average Weekly Earnings Ex. Bonus slowed to +3.1% y/y (3 mths to Jan.)

Other

- PBoC unexpectedly on hold
- RBA cuts 25 bps to 0.25%, starts QE; RBNZ slashes 75 bps to 0.25% in emergency moves
- Brazil cuts 50 bps to 3.75%

Good News

Australia—Employment +26,700 (Feb.)—and **Jobless Rate** -0.2 ppts to 5.1%

Bad News

China—Industrial Production -13.5% y/y (Jan.-Feb.)

China—Retail Sales -20.5% y/y (Jan.-Feb.)

China—Fixed Asset Investment -24.5% y/y (Jan.-Feb.)

Tracking the Pandemic's Economic Footprint

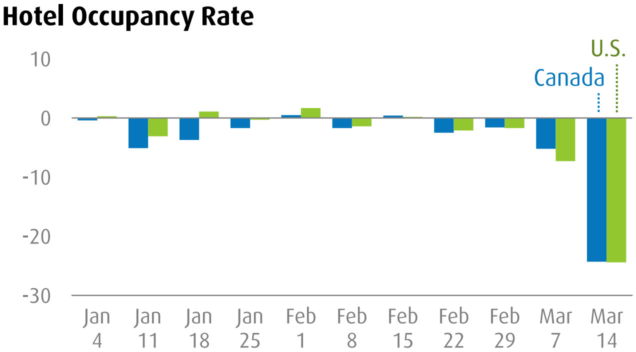
Sal Guatieri and Erik Johnson

As vast parts of the global economy shut down in order to control the outbreak of the coronavirus, analysts will be watching a number of timely indicators to track the scope and speed of the disruptions. Equally important will be identifying the hoped for speedy recovery in response to pent-up demand and aggressive policy stimulus once the outbreak subsides. While the focus of this article is on the U.S. economy given more readily available **weekly** and **daily** data, the trends here are likely to apply to Canada, which is also dealing with an oil-price shock.

Several high-frequency indicators worth watching are:

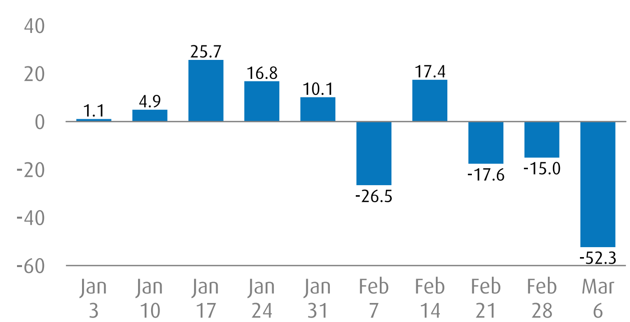
- **Hotel Occupancy**: As planned vacations and conferences are postponed or cancelled, and most air travel is grounded, the hospitality industry is quickly seeing its revenue sources dry up. Average weekly hotel occupancy in Canada and the United States has already fallen sharply (*Chart 1*). For the week ending March 14, occupancy was off by 24% in both countries. We're likely to see substantial layoffs in the sector if Glassdoor's job openings survey for the week ending March 13 is indicative of what is to come. It showed an 18% w/w decline in postings for leisure and hospitality. Extended UI measures by the government will be important for maintaining local spending levels in metro areas, which rely on hospitality, as labour demand is pulling back in a big way.
- **Cinema tickets**: After last week's sharp decline in domestic box office gross (*Chart 2*), most major studios have pulled the rest of their upcoming films for the foreseeable future. The majority of major cinemas have closed for the time being to mitigate the spread of the virus. The past week's sales were off 69% y/y. That's a broader sign that a number of consumable-service categories are facing a sudden stop.
- **Restaurant visits**: As fears over the spread of COVID-19 heightened by the end of last week, the restaurant industry began to see an immense drop-off in volumes, particularly in areas with higher confirmed cases (*Charts 3 and 4*). By Wednesday, after forced closures, a number of cities across Canada and the U.S. were reporting a 100% reduction in restaurant activity. While UI benefits will help support laid-off workers, tips are an important source of income for this group, and they are not counted as insurable earnings. This could have cascading effects in affected areas, as

Chart 1
~~No~~ Vacancy
2020 (y/y % chng)
Hotel Occupancy Rate



Sources: BMO Economics, STR

Chart 2
Bad Ending
2020 — United States (US$: y/y % chng by week)
Domestic Box Office Gross



Sources: BMO Economics, BoxOfficeMojo

reductions in income lead to missed rent payments; and, in turn, missed mortgage payments. Forbearance measures to mitigate a downward spiral will be crucial for limiting the economic hardship.

- **Search trends:** Google query activity suggests that the upcoming initial claims data (next week) will be of historic proportion. Search activity for unemployment on March 15 was up 162% in the U.S. and 115% in Canada compared to their averages over the past year. It will be crucial for the public service to keep up with the administrative load in order to quickly replace lost income.

Along with the above real-time indicators, it will be worth monitoring several weekly series, including:

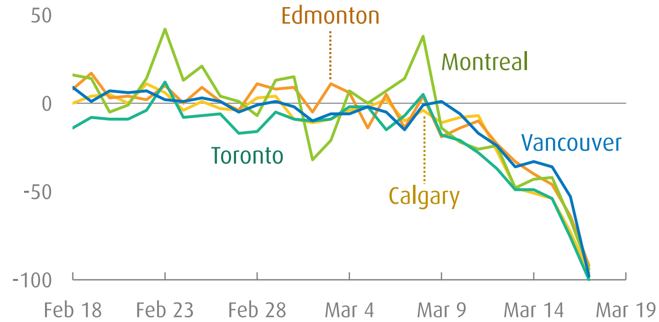
- **Jobless claims:** Stemming the coming wave of layoffs and loss of income is crucial if the economy is to avoid a prolonged contraction and sluggish recovery. Until recently, U.S. initial claims were perched near half-century lows, but they shot up 70,000--more than during the Great Recession--to a 2½-year high of 281,000 last week (*Chart 5).* Claims trended higher after 9/11 and Hurricane Katrina, and they will easily surpass the Great Recession peak of 665,000. Estimates put the total reported claims from state agencies at 2.5 million for the current week. In Canada, 500,000 have applied for EI this week compared to the typical 27,000. Proposed government support measures should help some businesses to continue paying workers without resorting to layoffs, but many will need to turn to unemployment insurance for support.

- **Consumer confidence**: Sentiment will depend on the course of the outbreak, the number of layoffs, and the scope of the equity-market correction. If it is shattered for any length of time, spending will retrench sharply and take longer to recover. The University of Michigan publishes household sentiment figures every two weeks. The early March report showed a large crack in confidence, with the index sliding five points from two-year highs (*Chart 6*). Unsurprisingly, the expectations component took the brunt of the hit given fears that the outbreak will worsen and cause a severe recession. If history is a guide, the index will decline much further. However, when households sense the worst is over, the expectations component should lead an improvement in sentiment, and likely spending.

Chart 3
Eating In

2020 — Canada (y/y % chng)

Restaurant Diners

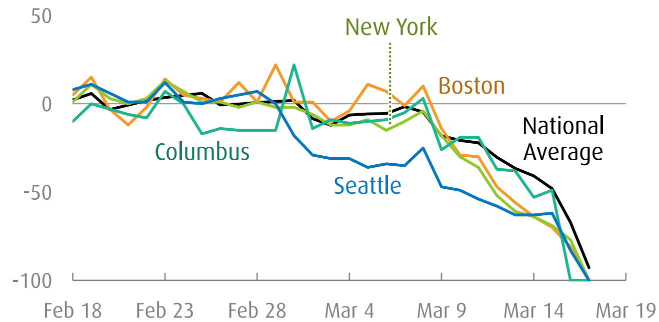


Sources: BMO Economics, OpenTable Data Center

Chart 4
Table for 0

2020 — United States (y/y % chng)

Restaurant Diners

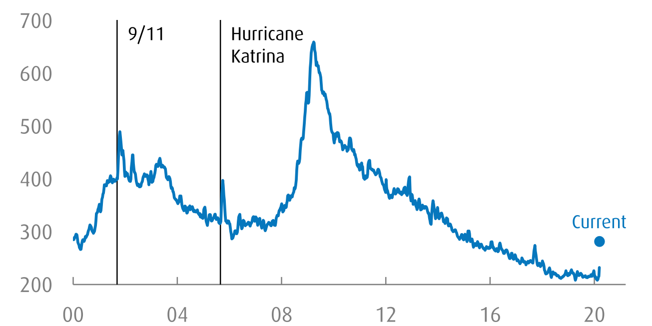


Sources: BMO Economics, OpenTable Data Center

Chart 5
Claims Spike Higher After Disasters...

United States (000s : s.a. : 4-wk m.a.)

Unemployment Insurance: Initial Claims

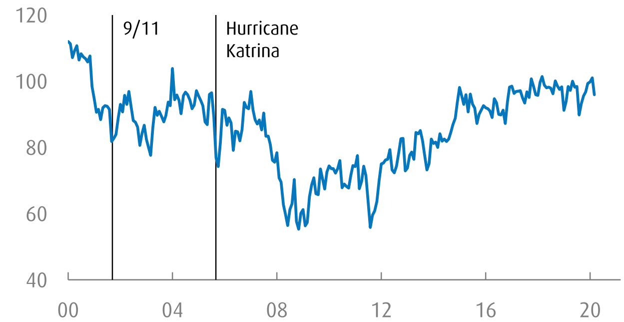


Sources: BMO Economics, Haver Analytics

Chart 6
...And Confidence Takes a Hit

United States (1966:Q1 = 100 : n.s.a.)

University of Michigan: Consumer Sentiment



Sources: BMO Economics, Haver Analytics

- **Mortgage applications**: Weekly mortgage refinancings have shot higher due to the historic plunge in mortgage rates. This will help put extra dollars in people's pockets. But, it's loans for home purchases that should be eyed to gauge the impact of the virus on the housing market. While applications for purchases rose in early March due to the previously strengthening market, they pulled back last week, and will slide as buyer confidence tumbles. Only after buyers sense the coast is clear are they likely to jump back into the market.
- **Retail sales**: Johnson Redbook retail sales vaulted 8.5% y/y higher in the second week of March due to stockpiling as news of the pandemic spread. However, social distancing will drive sales sharply lower in coming weeks. Sales tumbled in the weeks after 9/11, and they will take longer to bounce back this time.
- **Steel production:** U.S. steel production was already sliding earlier this year after rising in late 2019, and reached a 1½-year low last week. The industry will be hit by disruptions to materials (e.g., iron ore) and demand, especially now that most major automakers have closed their doors until at least month's end.
- **Oil production:** After averaging a record daily high of almost 13 million barrels per day in January, U.S. crude production steadied in the first half of March amid plunging demand from China. While China's factories are starting to reopen, demand in the rest of the world is careening lower. Moreover, with prices recently touching 18-year lows, many smaller oil producers could be forced out of business.

Bottom Line: The above indicators will provide a timely view on the economic dislocations still to come, helping to guide "guesstimates" of quarterly GDP. We currently see U.S. GDP contracting 10% annualized in Q2. If there is an upside to the dismal data coming down the pipe, it's that they will suggest that people are taking social distancing seriously. If we are able to flatten the epidemic curve sooner, then the economy will stand a better chance of rebounding by the summer. These indicators should help to identify that turning point.

Economic Forecast Summary for March 20, 2020

	2019				2020				Annual		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2018	2019	2020
CANADA											
Real GDP (q/q % chng : a.r.)	1.0	3.4	1.1	0.3	-2.5 ↓	-10.0 ↓	7.5 ↑	4.5 ↑	2.0	1.6	-1.0 ↓
Consumer Price Index (y/y % chng)	1.6	2.1	1.9	2.1	2.0	0.7 ↓	1.1 ↓	1.2 ↓	2.3	1.9	1.2 ↓
Unemployment Rate (percent)	5.8	5.6	5.6	5.7	5.9 ↑	7.3 ↑	6.9 ↑	6.7 ↑	5.8	5.7	6.7 ↑
Housing Starts (000s : a.r.)	187	224	223	202	209	205	206	204	214	209	206
Current Account Balance ($blns : a.r.)	-69.4	-33.7	-43.5	-35.0	-53.7 ↓	-73.8 ↓	-69.0 ↓	-63.7 ↓	-55.5	-45.4	-65.0 ↓
Interest Rates					(average for the quarter : %)						
Overnight Rate	1.75	1.75	1.75	1.75	1.25 ↓	0.25	0.25	0.25	1.44	1.75	0.50 ↓
3-month Treasury Bill	1.65	1.67	1.64	1.66	1.30	0.25	0.20	0.20	1.37	1.65	0.50
10-year Bond	1.86	1.62	1.36	1.52	1.20	0.65 ↑	0.70 ↑	0.80	2.28	1.59	0.85 ↑
Canada-U.S. Interest Rate Spreads					(average for the quarter : bps)						
90-day	-79	-68	-38	5	13 ↓	6	3	3	-60	-45	6
10-year	-80	-72	-43	-28	-19 ↑	-6 ↓	-5 ↓	-4 ↓	-63	-56	-8 ↓
UNITED STATES											
Real GDP (q/q % chng : a.r.)	3.1	2.0	2.1	2.1	-2.0 ↓	-10.0 ↓	7.0 ↑	5.0 ↑	2.9	2.3	-0.5 ↓
Consumer Price Index (y/y % chng)	1.6	1.8	1.8	2.0	2.1	0.5 ↓	0.6 ↓	0.5 ↓	2.4	1.8	0.9 ↓
Unemployment Rate (percent)	3.9	3.6	3.6	3.5	3.7 ↑	5.0 ↑	4.8 ↑	4.5 ↑	3.9	3.7	4.5 ↑
Housing Starts (mlns : a.r.)	1.21	1.26	1.28	1.44	1.53 ↑	1.29 ↓	1.33 ↓	1.35 ↓	1.25	1.30	1.38 ↓
Current Account Balance ($blns : a.r.)	-548	-505	-502	-439	-441 ↓	-395 ↓	-396 ↓	-409 ↓	-491	-498	-410 ↓
Interest Rates					(average for the quarter : %)						
Fed Funds Target Rate	2.38	2.38	2.13	1.63	1.13 ↓	0.13	0.13	0.13	1.83	2.13	0.38 ↓
3-month Treasury Bill	2.44	2.35	2.02	1.61	1.15	0.20	0.20	0.20	1.97	2.10	0.45
10-year Note	2.65	2.33	1.79	1.79	1.40	0.70 ↑	0.75 ↑	0.85 ↑	2.91	2.14	0.90 ↑
EXCHANGE RATES					(average for the quarter)						
US¢/C$	75.2	74.8	75.7	75.8	74.0 ↓	67.1 ↓	68.8 ↓	70.8 ↓	77.2	75.4	70.2 ↓
C$/US$	1.33	1.34	1.32	1.32	1.35 ↑	1.49 ↑	1.45 ↑	1.41 ↑	1.30	1.33	1.43 ↑
¥/US$	110	110	107	109	109 ↑	102	102	106	110	109	105 ↑
US$/Euro	1.14	1.12	1.11	1.11	1.10 ↓	1.08 ↓	1.08 ↓	1.10	1.18	1.12	1.09 ↓
US$/£	1.30	1.29	1.23	1.29	1.27 ↓	1.17 ↓	1.17 ↓	1.19 ↓	1.34	1.28	1.20 ↓

Blocked areas mark BMO Capital Markets forecasts; up and down arrows (↑↓) indicate forecast changes; spreads may differ due to rounding

Canada

There are no key releases for the coming week.

United States

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416-359-4747

New Home Sales

Tuesday, 10:00 am

Feb. (e)	**756,000 a.r.**	**(-1.0%)**
Consensus	*750,000 a.r.*	*(-1.8%)*
Jan.	764,000 a.r.	(+7.9%)

The COVID-19 crisis' hits to consumer confidence and household income growth should majorly dampen housing demand this month. Would-be home buyers' desires to traipse through builders' presentation centres or strangers' homes for sale are going to wane profoundly, particularly against a backdrop of social distancing. However, last month's new home sales still likely garnered some support from the combination of still-firming housing demand (at least in the first part of the month) and record-low existing homes for sale. Homebuilders reported elevated current sales; the respective component in the Housing Market Index matched its second highest level in more than two decades. However, it was wetter than typical, and there could be some payback for January's jump (7.9% to 764k, which was the highest in more than 12 years). On balance, we look for a slight 1.0% dip to 756k.

Durable Goods Orders

Wednesday, 8:30 am

		Ex. Transport
Feb. (e)	**+0.9%**	**-0.4%**
Consensus	*-1.0%*	*-0.4%*
Jan.	-0.2%	+0.8%

	Nondef. Cap. Goods ex. Air
Feb. (e)	**-0.4%**
Consensus	-0.4%
Jan.	+1.1%

February is typically the weakest month of the year when it comes to aircraft and parts orders, and Boeing's suspension of 737 MAX production in the prior month is going to make matters worse. However, Boeing did book 18 new orders in the month, when rival Airbus had none. This should provide a lift to total durable goods orders in February (seasonally adjusted). But, apart from the aircraft sector, we look for a fractionally lower figure as concerns over Chinese supply chains crimped by COVID-19—and emerging concerns over how the virus might eventually impact U.S. demand—moved quickly to replace concerns over the global trade war in the minds of purchasing managers and capex decision-makers. Non-defense capital goods (ex-aircraft) orders also likely slipped around 0.4%, after January's large 1.1% jump.

Personal Spending & Income

Friday, 8:30 am

	Personal Spending	**Personal Income**
Feb. (e)	**+0.1%**	**+0.5%**
Consensus	*+0.3%*	*+0.4%*
Jan.	+0.2%	+0.6%

	Core PCE Price Index	
Feb. (e)	**+0.2%**	**+1.8% y/y**
Consensus	*+0.2%*	*+1.8% y/y*
Jan.	+0.1%	+1.6% y/y

Retail sales registered broad-based weakness in February. Although the headline was expected to be braked by slower vehicle sales and lower gasoline prices, the 0.2% slip in sales ex-autos & gas along with the flat reading for the control measure (ex-autos, gas, food services & building materials)—the latter feeding into PCE—was unexpectedly weak. This suggests some spending caution owing to COVID-19 was already surfacing last month, which also probably spilled over into other services. We judge total PCE might edge up only 0.1% nominally, for a flat real reading. Interestingly, the core PCE price index should increase 0.2%, raising the core rate to 1.8% y/y—a 13-month high unrounded—but a complete non-event amid the emerging coronavirus crisis. Personal income should increase a firm 0.5% in February, supported by back-to-back 273k payroll job gains, and pushing the personal savings rate up to 8.3% from 7.9%. But, as job layoffs spread in the weeks ahead, both income growth and the savings rate are going to subside a lot.

Financial Markets Update for March 20, 2020

		Mar 20 [1]	Mar 13	Week Ago	4 Weeks Ago	Dec 31, 2019
					(basis point change)	
Canadian Money Market	Call Money	0.75	0.75	0	-100	-100
	Prime Rate	2.95	3.45	-50	-100	-100
U.S. Money Market	Fed Funds (effective)	0.25	1.25	-100	-150	-150
	Prime Rate	3.25	4.25	-100	-150	-150
3-Month Rates	Canada	0.44	0.61	-17	-119	-122
	United States	-0.02	0.24	-26	-156	-156
	Japan	-0.28	-0.30	2	-14	-17
	Eurozone	-0.37	-0.43	6	4	1
	United Kingdom	0.54	0.51	3	-21	-26
	Australia	0.52	0.62	-11	-37	-40
2-Year Bonds	Canada	0.56	0.53	3	-86	-113
	United States	0.35	0.49	-14	-100	-122
10-Year Bonds	Canada	0.91	0.85	6	-37	-79
	United States	0.95	0.96	-1	-52	-97
	Japan	0.06	0.02	4	12	8
	Germany	-0.33	-0.55	22	10	-14
	United Kingdom	0.55	0.41	14	-3	-27
	Australia	1.14	0.98	16	20	-23
Risk Indicators	VIX	63.2	57.8	5.4 pts	46.1 pts	49.4 pts
	TED Spread	122	60	62	109	85
	Inv. Grade CDS Spread [2]	137	120	17	91	92
	High Yield CDS Spread [2]	755	611	144	459	475
					(percent change)	
Currencies	US¢/C$	69.68	72.43	-3.8	-7.8	-9.5
	C$/US$	1.435	1.381	—	—	—
	¥/US$	111.26	107.62	3.4	-0.3	2.4
	US$/€	1.0686	1.1107	-3.8	-1.5	-4.7
	US$/£	1.176	1.228	-4.2	-9.3	-11.3
	US¢/A$	58.48	62.03	-5.7	-11.8	-16.7
Commodities	CRB Futures Index	125.49	140.84	-10.9	-28.1	-32.5
	Oil (generic contract)	22.39	31.73	-29.4	-58.1	-63.3
	Natural Gas (generic contract)	1.61	1.87	-13.8	-15.4	-26.4
	Gold (spot price)	1,490.75	1,529.83	-2.6	-9.3	-1.7
Equities	S&P/TSX Composite	12,507	13,716	-8.8	-29.9	-26.7
	S&P 500	2,403	2,711	-11.3	-28.0	-25.6
	Nasdaq	7,200	7,875	-8.6	-24.8	-19.8
	Dow Jones Industrial	20,135	23,186	-13.2	-30.5	-29.4
	Nikkei	16,553	17,431	-5.0	-29.2	-30.0
	Frankfurt DAX	8,961	9,232	-2.9	-34.0	-32.4
	London FT100	5,187	5,366	-3.3	-29.9	-31.2
	France CAC40	4,062	4,118	-1.4	-32.6	-32.0
	S&P ASX 200	4,817	5,539	-13.0	-32.5	-27.9

[1] = as of 12:00 pm *[2] = One day delay*

	Monday March 23	Tuesday March 24	Wednesday March 25	Thursday March 26	Friday March 27
Japan		**Manufacturing PMI** **Mar. P** Feb. 47.8 **Services PMI** **Mar. P** Feb. 46.8 **Composite PMI** **Mar. P** Feb. 47.0 **Department Store Sales** **Feb.** Jan. -3.1% y/y			
Euro Area	**EURO AREA** **Consumer Confidence** **Mar. A (e) -13.6** Feb. -6.6	**EURO AREA** **Manufacturing PMI** **Mar. P (e) 40.0** Feb. 49.2 **Services PMI** **Mar. P (e) 40.0** Feb. 52.6 **Composite PMI** **Mar. P (e) 38.9** Feb. 51.6	**GERMANY** **ifo Business Climate** **Mar. F (e) 87.7** Feb. 96.0	**EURO AREA** **M3 Money Supply** **Feb. (e) +5.2% y/y** Jan. +5.2% y/y **ECB Economic Bulletin** **GERMANY** **GfK Consumer Confidence** **Apr. (e) 8.2** Mar. 9.8 **FRANCE** **Business Confidence** **Mar. (e) 94** Feb. 105	**GERMANY** **Retail Sales** [D] **Feb. (e) unch +1.5% y/y** Jan. +1.0% +2.1% y/y **FRANCE** **Consumer Confidence** **Mar. (e) 92** Feb. 104 **ITALY** **Consumer Confidence** **Mar. (e) 100.0** Feb. 111.4
U.K.		**Manufacturing PMI** **Mar. P (e) 45.0** Feb. 51.7 **Services PMI** **Mar. P (e) 45.0** Feb. 53.2 **Composite PMI** **Mar. P (e) 45.1** Feb. 53.0	**Consumer Price Index** **Feb. (e) +0.3% +1.6% y/y** Jan. -0.3% +1.8% y/y **Core CPI** **Feb. (e) +1.5% y/y** Jan. +1.6% y/y **Producer Price Index (Output)** **Feb. (e) unch +0.9% y/y** Jan. +0.3% +1.1% y/y	**Retail Sales (incl. Fuel)** **Feb. (e) +0.2% +0.7% y/y** Jan. +0.9% +0.8% y/y **8:00 am ET BoE Policy Announcement**	
Other				**MEXICO** **Central Bank of Mexico Monetary Policy Meeting**	

D = date approximate

Upcoming Policy Meetings | Bank of England: May 7, June 18, Aug. 6 | European Central Bank: Apr. 30, June 4, July 16

Monday March 23

Canada

8:30 am	**Wholesale Trade**	
Jan. (e)	**+0.3%**	
Dec.	+0.9%	

United States

8:30 am	**Chicago Fed National Activity Index**	
Feb.		
Jan.	-0.25	
11:30 am	13- & 26-week bill auctions $84 bln	

Tuesday March 24

United States

9:45 am	**Markit PMIs (Mar. P)**	
10:00 am	**New Home Sales**	
Feb. (e)	**756,000 a.r. (-1.0%)**	
Consensus	*750,000 a.r. (-1.8%)*	
Jan.	764,000 a.r. (+7.9%)	
10:00 am	**Wholesale Inventory Revisions**	
10:00 am	**Richmond Fed Manufacturing Index**	
Mar. (e)	**-10**[C]	
Feb.	-2	
11:00 am	4- & 8-week bill auction announcements	
11:30 am	52-week bill auction $26 bln	
1:00 pm	2-year note auction $40 bln	

Wednesday March 25

Canada

Ontario Fiscal Update

United States

7:00 am	**MBA Mortgage Apps**	
Mar. 20		
Mar. 13	-8.4%	
8:30 am	**Durable Goods Orders**	**Ex. Transport**
Feb. (e)	**+0.9%**	**-0.4%**
Consensus	*-1.0%*	*-0.4%*
Jan.	-0.2%	+0.8%
8:30 am	**Nondef. Cap. Goods ex. Air**	
Feb. (e)	**-0.4%**	
Consensus	*-0.4%*	
Jan.	+1.1%	
9:00 am	**FHFA House Price Index**	
Jan. (e)	**+0.6%**	**+5.2% y/y**
Consensus	*+0.4%*	*+5.0% y/y*
Dec.	+0.6%	+5.2% y/y
11:30 am	2[R]-year FRN auction $18 bln	
1:00 pm	5-year note auction $41 bln	

Thursday March 26

Canada

Noon	2-year bond auction $5 bln

United States

8:30 am	**Initial Claims**	
Mar. 21 (e)	**1,100k (+819k)**[C]	
Mar. 14	281k (+70k)	
8:30 am	**Continuing Claims**	
Mar. 14		
Mar. 7	1,701k (+2k)	
8:30 am	**Real GDP**	**GDP Deflator**
Q4 F (e)	**+2.1% a.r.**	**+1.3% a.r.**
Consensus	*+2.1% a.r.*	*+1.3% a.r.*
Q4 P	+2.1% a.r.	+1.3% a.r.
Q3	+2.1% a.r.	+1.8% a.r.
8:30 am	**Pre-Tax Corporate Profits**	
Q4 (e)	**+0.5% y/y**	
Q3	-1.2% y/y	
8:30 am	**Goods Trade Deficit**	
Feb. A (e)	**$63.8 bln**[C]	
Jan.	$65.9 bln	
8:30 am	**Wholesale and Retail Inventories (Feb. A)**	
11:00 am	**Kansas City Fed Manufacturing Activity**	
Mar. (e)	**-8**[C]	
Feb.	5	
11:00 am	13- & 26-week bill auction announcements	
11:30 am	4- & 8-week bill auctions	
1:00 pm	7-year note auction $32 bln	

Friday March 27

Canada

8:30 am	**Survey of Employment, Payrolls, and Hours (Jan.)**
Ottawa's Budget Balance[D]	
Jan. '20	
Jan. '19	-$1.5 bln

United States

8:30 am	**Personal Spending**	**Personal Income**
Feb. (e)	**+0.1%**	**+0.5%**
Consensus	*+0.3%*	*+0.4%*
Jan.	+0.2%	+0.6%
8:30 am	**Core PCE Price Index**	
Feb. (e)	**+0.2%**	**+1.8% y/y**
Consensus	*+0.2%*	*+1.8% y/y*
Jan.	+0.1%	+1.6% y/y
10:00 am	**University of Michigan Consumer Sentiment**	
Mar. F (e)	**92.5**[C]	
Mar. P	101.0	
Feb.	95.9	

Sunday March 29

Puerto Rico Democratic Primary (51 delegates)

[C] = consensus [D] = date approximate [R] = reopening

Upcoming Policy Meetings | Bank of Canada: Apr. 15, June 3, July 15 | FOMC: Apr. 28-29, June 9-10, July 28-29

General Disclosures

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