Coronavirus, Global Markets and Global GDP

As CNN stated so perfectly: "You can't make a car with 99% of the parts."

On Friday, January 24, 2020 news of a second case of coronavirus in the U.S. pushed the stock market down 1% as investors scrambled for the cover of perceived safer assets, including U.S. Treasuries.

The stock markets in the U.S. shook off negative numbers from the week ending January 24th and the following week ending January 31st, by jumping to new highs as investors seemed to think the coronavirus was contained. In one week's time, the NASDAQ leapt 4.0% and the S&P 500 and DJIA each moved up 3.2% and 3.0%, respectively.

But also in those two weeks' time, the World Health Organization announced that there were over 40,000 confirmed cases and 1,000 confirmed deaths. And Tedros Adhanom Ghebreyesus, director-general of the World Health Organization, warned that those numbers may just be the start.

"There've been some concerning instances of spread from people with no travel history to China," Tedros said. "The detection of a small number of cases may indicate more widespread transmission in other countries. In short, we may only be seeing the tip of the iceberg."

China Is a Global Supplier

As the coronavirus continues to spread around the world, investors are worried that the Chinese virus will impact markets in the U.S. and around the globe. The reality is that China is an integral part of the global supply chain and is considered to be the world's factory – from iPhones to car parts.

But beyond China as the world's supplier, consider the flip side of China's economy too – that of the world's largest consumer group based on sheer numbers. Yes, the U.S. has the world's largest consumer market in terms of spending dollars, but China is number two. And China is the world's fastest growing consumer market.

Further, not only does China have millions of very wealthy consumers that buy luxury products, go on extravagant trips and buy cars, but China's growth has also driven demand for commodities like copper, steel and soybeans. In fact, roughly 15 years ago, China's economy accounted for about 4% of the world's GDP. Today it accounts for 16%.

The Auto Industry is Suffering

Car plants across China have been ordered to remain closed following the Lunar New Year holiday, and this is impacting these global brands:

- Toyota
- Volkswagen
- Hyundai
- General Motors

And not only can these car makers not resume operations in the world's largest car market, but these are also the top 4 car makers in the entire world.

Making matters worse is that China is a massive supplier of parts to auto plants around the world. In fact, the UN estimates that China shipped nearly $35 billion in auto parts out last year, with about $20 billion being sent to the U.S. alone. And a recent CNN headline summed up the issue best:

"You can't make a car with 99% of the parts."

In other words, a single missing part could paralyze the entire assembly line.

Earnings Impacted?

Industries that you might expect to be impacted are being impacted. Here are just a few more:

- Airline stocks. Air China and China Eastern for sure, but American Airlines, Delta Air Lines and British Airways have suspended all flights to and from China
- Cruise line operators. Royal Caribbean and other cruise lines are slumping as global tourism is impacted
- Luxury good makers. Burberry has closed half of its 64 stores in China and Capri Holdings and Estee Lauder are issuing earnings warnings
- Gaming stocks. Wynn Resorts said it's losing $2.6 million each day
- Starbucks, Apple, Nike and Disney have all issued warnings on how the virus might impact their earnings

Stunningly, according to data from natural language processor Amenity Analytics, 421 different global companies have indicated that the coronavirus could negatively impact financial results for the first quarter. And of those 421 companies, 394 of them are based in the U.S.

Impact for Investors

The economic fallout from the coronavirus will impact travel, trade, financial networks and just about every single sector one way or another. For sure, the virus will impact China's economy, potentially shaving off a percentage point to its first quarter GDP numbers. Whether the impact will be short- or long-term depends on the extent of the outbreak of course.

But before you start unloading your exposure to travel, auto and airline sectors; and before you start stocking up on healthcare stocks; and before you start eliminating your exposure to emerging markets in favor of more developed markets; and before you start moving out of equities into short-term Treasuries, discuss with your advisor.

In fact, before you make any changes to your portfolio allocations, make sure you examine the impact it might have to your overall portfolio and risk profile, as well as any tax implications that you might create.

Your advisor can help guide you through this analysis.