



R&R Weekly Column
By Brunello Rosa



Loss Minimization Is The Correct Business Strategy For Coronavirus

We have discussed the [macroeconomic impact](#) of Coronavirus in [several recent columns](#) and [research pieces](#). It is clear that we have already started witnessing large falls in economic activity around the globe in Q1. In some countries, GDP had fallen already 4-5% on a quarterly basis, and the collapse of real GDP growth will be in double digits in Q2. As a result, [oil prices have collapsed into negative territory for the first time ever](#). Unemployment rates are soaring everywhere, with the [US having witnessed a 30mn rise in initial jobless claims](#) in the last six weeks, wiping out the gains made over the past several years.

Governments and central banks are coming to the [rescue with large stimulus packages](#), but these will still struggle to reach small and medium sized enterprises (SMEs) and the self-employed, which will be decimated by the crisis. [Helicopter money works only if money reaches every corner of the system](#), without remaining concentrated in the hands of a lucky few and without remaining concentrated in intermediary institutions such as banks.

When economies and societies do re-open, nothing will be like it was before. We will have to live together with the virus for so many months, potentially for another year until a vaccine becomes available on a large scale for most of the global population. Until that time social distancing will remain the mantra in most work and business environments. Teams might need to work on alternate days or weeks. Open-space offices will remain unfilled for the months to come. In the aviation industry, planes will fly half empty and airports will devote much larger spaces to passengers. In the hospitality industry, restaurants will have to find ways to serve food while complying with social distancing regulations, and hotels will remain half empty at best.

In such an environment, what is the right strategy to adopt in order for your business to survive? Well, during the financial crisis, [Richard Koo's theory of "balance sheet recession" got a lot of attention](#). It was based on the fact that, in a financial crisis, private sector agents are trying to deleverage, and therefore the only entity able to increase its debts is the government. In such an environment, private sector agents switch from being profit-maximisers to become debt-minimizers, to regain financial viability.

In this crisis, unless private-sector agents receive grants from public authorities, they will need to take loans, which banks will offer at a very cheap rate and with favourable conditions as a result of central bank's credit-easing measures. In this crisis, therefore, private-sector agents cannot afford to be debt-minimizers. Also, especially companies should forget about being profit maximisers, in order to avoid frustration and disappointment. In an environment such as the one described above, they will be forced to run at half-capacity at best and therefore they will surely suffer losses.

Since losses will come no matter what, the ideal business strategy to adopt is to minimize such losses, without regretting too much the lost revenues and profits. Most of those losses, especially in public services, will likely be subsidised by the government. In some cases, subsidization will not be possible, and so the aim should be to develop enough internal efficiencies to minimise future losses. The development of the various forms of remote working point exactly in that direction.

Our Recent Publications

[Flash Previews: BOE, RBA And Norges Bank Likely To Keep Their Interest Rates Unchanged, While Re-Assessing Their Overall Policy Stance](#), by Brunello Rosa, Fawaz Al Mughrabi, Farah Aladsani and Karmen Meneses, 1 May 2020

[Flash Review: ECB Eases Further Credit Conditions And Opens To Wider And Larger PEPP](#), By Brunello Rosa, 30 April 2020

[Flash Review: Fed Believes Current Stance is "Appropriate", But It's Ready To Do More](#). By Brunello Rosa, 29 April 2020

[Flash Reviews: BOJ And Riksbank Remain Very Accommodative Facing An Uncertain Economic Outlook](#), by Brunello Rosa and Fawaz Al Mughrabi, 28 April 2020

[Flash Preview: ECB To Expand The Scope \(And Possibly The Size\) of PEPP in April](#). By Brunello Rosa and Nouriel Roubini, 28 April 2020

[Q2-2020 STRATEGIC ASSET ALLOCATION - Focus On The Long-Term, Find Opportunities In The Crisis](#). By Alessandro Magnoli Bocchi, Nouriel Roubini, Fawaz Sulaiman Al Mughrabi, Farah Aladsani, 27 April 2020

[Flash Preview: Fed To Maintain Its Very Easy Monetary and Credit Stance And Stand Ready To Do More](#). By Nouriel Roubini and Brunello Rosa, 27 April 2020

Looking Ahead

The Week Ahead: US Will Show Employment Destruction

In the US, April labor market data will show 'employment destruction', as: *i*) nonfarm payrolls could decline by -21m (p: -0.7m); *ii*) unemployment will likely rise to 16.0% (p: 4.4%); while *iii*) average hourly earnings could rise by 3.3% y-o-y (p: 3.1), as layoffs are concentrated in lower-earning jobs.

The Quarter Ahead: Despite The Policy Response, The Re-Start of Economic Activity Will Remain Slow Until A Vaccine Is Produced

Containment measures could be relaxed as infection cases peak in **several countries**, but recent experiences suggest: *i*) a very slow recovery in demand (**China**); and *ii*) "second wave" risks could force policymakers to reinstate 'lockdown measures' (**Singapore**).

In the US, President Trump attacked China over 'its role in the spread of COVID-19', and raised the prospects of 'trade tariffs'. Fed's Chair Powell highlighted 'considerable risks' to the medium-term outlook, such as: *i*) the virus trajectory; *ii*) damage to productive capacity; and *iii*) the global dimension of the crisis. The Fed noted that it will maintain the current policy rate's 'target range' 'until (...) confident that the economy is on track to achieve the maximum employment and price stability goals'.

In the EZ, the ECB announced it is: *i*) 'fully prepared' to increase asset purchases, 'if needed'; *ii*) ready to extend the program beyond 2020, 'depending on the length of the crisis'; and *iii*) renewing its call for 'a coordinated EU fiscal response'.

In the UK, Australia, and Norway, CBs are expected to keep rates low at 0.10%, 0.25%, and 0.25%, respectively - while reasserting a supportive stance.

Last Week's Review

Real Economy: Significant Declines In Economic Output, Inflation Begins To Soften, Risks Rise

In the US, a decade-long expansion ended in Q1, when GDP contracted by -4.8% q-o-q annualized (c: -4.0; p: 2.1). An additional 3.8m workers (c: 3.5m; p: 4.4m) filed for jobless claims, bringing 'total initial claims' to over 30mn in six weeks. As jobs are lost, consumers cut back on spending (Personal spending Mar., a: -7.5% m-o-m; c: -5.0; p: 0.2). Services spending - accounting for 45% of GDP - declined at a -10.2% annualized rate, more than three times the steepest decline on record: -3.0% in Q4-1953. The PCE - a measure of expenditures in personal consumption - slowed in March to 1.3% y-o-y (p: 1.8), and core-PCE to 1.3% y-o-y (c: 1.6; p: 1.8). The Fed left its interest rate unchanged at 0.25%.

In the EZ, Q1 GDP contracted by -3.8% q-o-q (c: -3.5; p: 0.1) and -3.3% y-o-y (c: -3.1; p: 1.0), more than during the GFC. Three of the bloc's four largest economies suffered record drops: *i*) France (a: -5.8% q-o-q; c: -3.5; p: -0.1); *ii*) Spain (a: -5.2% q-o-q; c: -4.4; p: 1.8); and *iii*) Italy (a: -4.7% q-o-q; c: -5.0; p: -0.3); France and Italy entered a 'technical recession' (i.e. two consecutive quarters of negative economic growth). April inflation decelerated, due to lower energy prices (a: 0.4% y-o-y; c: 0.1; p: 0.7), and core inflation softened to 0.9% (c: 0.7; p: 1.0). The ECB: *i*) refrained from boosting its bond-buying program; but *ii*) offered new 'pandemic emergency longer-term refinancing operations' (PELTROs) to EZ banks - to lower the interest rate on TLTRO III loans below the deposit rate (-0.50%).

In China, April's Caixin manufacturing PMI unexpectedly fell back into contraction (a: 49.4; c: 50.3; p: 50.1), as global headwinds hamper the expected economic rebound. Inflation is softening.

In Japan, the BoJ: *i*) held its policy rate at -0.1%; *ii*) removed the JPY80tn cap on annual government bond purchases; and *iii*) increased its purchase target for corporate bonds.

In Sweden, Riksbank kept its repo rate at 0% and hinted that "balance-sheet measures are likely to be the preferred method" for policy support.

Financial Markets: Volatility Rises, Due To Geopolitical Tensions And Weak Corporate Earnings

Market drivers: investors looked beyond economic data, focusing on a recovery led by: *i*) new therapy announcements; *ii*) hopes for a vaccine breakthrough; and *iii*) supportive policies.

Stocks: w-o-w, global indices rose (MSCI ACWI, +1.3%, to 479), driven by the EZ (Euro Stoxx 50, +4.2% to 2,928) and EMs (MSCI EMs, +4.2% to 917). US equities fell on Friday, wiping out gains for the week (S&P 500, -0.2% to 2,831), after: *i*) profit warnings from Amazon and Apple; and *ii*) escalating US-China tensions.

Bonds: w-o-w, returns rose marginally (BAML Global, +0.1% to 292.8); yields fell in the EZ (German bunds, -11 bps to -0.58%; French OAT, -13 bps to -0.10%). The Fed's intervention in corporate bond markets triggered record highs for IG issuances.

FX: w-o-w, demand for USD weakened (DXY, -1.3% to 99.079) as other reserve (EUR/USD, +1.5% to 1.0098; GBP, +1.1% to 1.25) and EM currencies (MSCI EM FX index, +0.9% to 1,569) strengthened.

Commodities: Oil prices recovered from last week's lows (Brent, +23.3% to 26.4 USD/b; WTI, +16.8% to 16.9 USD/b).



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Abbreviations, Acronyms and Definitions

a	Actual	LN	Northern League, Italy
AKP	Justice and Development Party, Turkey	MSS	Five Star Movement, Italy
ann.	annualized	m-o-m	Month-on-month
ARS	Argentinian Peso	mb	Million barrels
avg.	Average	mb/d	Million barrels per day
bn	Billion	MENA	Middle East and North Africa
BoC	Bank of Canada	MHP	Nationalist Movement Party, Turkey
BoE	Bank of England	mn	Million
BoJ	Bank of Japan	MPC	Monetary Policy Committee
bpd	Barrels per day	NAFTA	North-American Free Trade Agreement
bps	Basis points	NATO	North Atlantic Treaty Organization
BS	Balance sheet	OECD	Organization for Economic Cooperation and Development
c	Consensus	Opec	Organization of Petroleum Exporting Countries
C/A	Current account	p	Previous
CB	Central bank	P2P	Peer-to-peer
CBB	Central Bank of Bahrain	PBoC	People's Bank of China
CBK	Central Bank of Kuwait	PCE	Personal Consumption Expenditures
CBT	Central Bank of Turkey	PE	Price to earnings ratio
CDU	Christian Democratic Union, Germany	PM	Prime minister
CNY	Chinese Yuan	PMI	Purchasing managers' index
CPI	Consumer Price Index	pps	Percentage points
DJIA	Dow Jones Industrial Average Index	pw	Previous week
DJEM	Dow Jones Emerging Markets Index	QCB	Qatar Central Bank
d-o-d	Day-on-day	QAR	Qatari Riyal
DXY	US Dollar Index	QE	Quantitative easing
EC	European Commission	q-o-q	Quarter-on-quarter
ECB	European Central Bank	RE	Real estate
ECJ	European Court of Justice	RBA	Reserve Bank of Australia
EIA	US Energy Information Agency	RRR	Reserve Requirement Ratio
EM	Emerging Markets	RUB	Russian Rouble
EP	European Parliament	SWF	Sovereign Wealth Fund
EPS	Earnings per share	tn	Trillion
EU	European Union	TRY	Turkish Lira
EUR	Euro	UAE	United Arab Emirates
EZ	Eurozone	UK	United Kingdom
Fed	US Federal Reserve	US	United States
FOMC	US Federal Open Market Committee	USD	United States Dollar
FRB	US Federal Reserve Board	USD/b	USD per barrel
FX	Foreign exchange	UST	US Treasury bills/bonds
FY	Fiscal Year	VAT	Value added tax
GCC	Gulf Cooperation Council	VIX	Chicago Board Options Exchange Volatility Index
GBP	British pound	WTI	West Texas Intermediate
GDP	Gross domestic product	WTO	World Trade Organisation
IMF	International Monetary Fund	w	Week
INR	Indian Rupee	w-o-w	Week-on-week
IPO	Initial public offering	y	Year
IRR	Iranian Rial	y-o-y	Year-on-year
JPY	Japanese yen	y-t-d	Year-to-date
k	thousand	ZAR	South African Rand
KSA	Kingdom of Saudi Arabia	2y; 10y	2-year; 10-year