LPL RESEARCH
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# ASSESSING CORONAVIRUS OUTBREAK

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After a three-and-a-half-month, largely uninterrupted rally in stocks, the period of calm ended last week as the coronavirus outbreak led to a bout of volatility. Though it is difficult to predict when the virus will be contained and how many more lives might be lost, we provide some historical perspective on other major global health events to help assess potential market impacts.

## BACKGROUND

On Monday, January 27, fears that the deadly coronavirus would spread further around the globe intensified and led to a 1.6% drop in the S&P 500 Index, the biggest one-day drop in the index since October 8, 2019. It was the first time the index had moved 1% in either direction since October 8—spanning 71 trading days—and ended a historically long 30-day streak without back-to-back declines. The eerie calm was bound to end at some point, and the virus outbreak did the trick. Selling pressure then intensified Friday.

So far, more than 200 deaths have been attributed to the disease out of nearly 10,000 cases, less deadly than SARS in 2003, which caused 774 deaths out of approximately 8,100 cases, or about four times the mortality rate. The low number of diagnosed cases in the United States along with the relatively low number of cases outside of China and Hong Kong (0.9% of total cases) is an encouraging sign. We are hopeful that the aggressive screening and containment measures, including leveraging new technologies, will help China contain the virus in the coming weeks.

## HISTORICAL COMPARISON

History shows us the market impact from similar events has tended to be modest and short-lived. We looked at prior outbreaks, including SARS, bird flu in 2005–06, and swine flu in 2009, for comparisons **[FIGURE 1]**.

**1 MAJOR GLOBAL HEALTH EVENTS SINCE 2002**

| | | Change in S&P 500 Index | | |
|---|---|---|---|---|
| Outbreak | WHO Emergency Global Alert Date | 1 Month | 3 Months | 6 Months |
| SARS | March 2003 | 2.3% | 24% | 27% |
| Bird flu | October 2005* | -2.1% | 2% | 5% |
| Swine flu | April 2009 | 11.3% | 8% | 30% |
| Ebola | October 2014 | 3.6% | 5% | 6% |
| Zika | February 2016 | 2.0% | 6% | 12% |
| Coronavirus | January 2020 | ? | ? | ? |

Source: LPL Research, World Health Organization, Credit Suisse, FactSet 01/29/20

* Public interest measured by google search trend data compiled by Credit Suisse.

We also included Ebola and Zika, but the regional concentration of Ebola in West Africa and the minimal loss of life from Zika made those cases less comparable (although we do not minimize the loss of a single life). The Middle East respiratory syndrome (MERS) was excluded as well because there were only two cases in the United States and no deaths. The U.S. stock market shrugged off all of these health scares and took cues from U.S. economic trends, which continued uninterrupted:

**SARS.** After the SARS outbreak in late 2002 and early 2003, which we consider the most comparable to the current coronavirus outbreak, the 2003–07 bull market began. The market reflected recovery from the 2001 recession and 2002 accounting scandals and the start of the Iraq War. The S&P 500 surged 24% in the three months after the World Health Organization (WHO) issued a global emergency alert. During that period, the Hang Seng Index in Hong Kong suffered a peak-to-trough decline of 14.8%, while the S&P 500 fell about 2% at its lowest point.

The temporary and modest loss of Chinese output during the second quarter of 2003 was quickly recovered in the third quarter of 2003, helped by Chinese government stimulus targeted toward the most-impacted travel-related businesses. There were no SARS-related deaths in the United States, and the U.S. economy was largely unaffected.

**Bird flu.** Stock market gains were more modest following the bird flu outbreak in 2005. Still, the S&P 500 managed gains of 2% and 5% over the subsequent three and six months after public interest in the disease peaked, based on Google search trends (source: Credit Suisse).

Economic impacts were quite limited even in affected Southeast Asia countries. Growth of Indonesian economic output slowed in 2005 but returned to trend in 2006, while growth in the Vietnamese economy continued uninterrupted.

**Swine flu.** Swine flu was the most deadly global health event in recent decades, with an estimated 200,000 deaths. That's a big and scary number. For perspective, however, WHO estimates that as many as 650,000 people die from the seasonal flu each year. As with the traditional flu, a tiny fraction of swine flu cases ended in death—just 1 per 5,000 cases.

During the three and six months following WHO's global emergency alert, the S&P 500 rallied 8% and 30%. This period coincided with the start of the current bull market as investors anticipated the end of the 2007–09 Great Recession and Global Financial Crisis. This outbreak had no noticeable impact on U.S. or global output.

## FOCUS ON FUNDAMENTALS

As with heightened geopolitical uncertainty related to the Middle East, fears that this deadly viral outbreak may spread further are understandably unsettling for investors. In addition it is always uncomfortable to talk about economic and market impact when dealing with human loss. Though we certainly don't want to be dismissive of the human toll, it's our job to provide historical economic and financial context which, we hope, provides reassurance and perspective.

As always, we continue to focus on the fundamentals of the economy, interest rates, and corporate profits. The generally favorable economic backdrop is the reason we were not sellers of stocks into weakness related to the U.S.-Iran conflict, nor are we sellers on the coronavirus outbreak. That doesn't mean we expect a smooth ride for markets. We recognize that strong gains late last year may limit potential advances this year.

With the S&P 500 having reached our estimated range of fair value for 2020 already, as we outlined in our *Outlook 2020*, we expect more volatility, even though we are encouraged by the stock market's ability to weather geopolitical and health risks.

A Federal Reserve (Fed) committed to keeping interest rates at current levels, which Fed Chair Jerome Powell reiterated at last week's policy meeting, along with progress on trade may improve prospects for business investment and productivity growth, and help power corporate profits higher. If stocks are going to move higher from here, we believe profits will be the key driver.

## WEEKLY MARKET PERFORMANCE REPORT

Please see our new *Weekly Market Performance* report with insights on major asset classes.

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