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Coronavirus Closes China to the World, straining Global Economy

By James T. Areddy
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SHANGHAI—China's isolation amid the coronavirus outbreak, a rare freeze out for such a vital economic center, is rippling across the world.
Uncertainty over the virus—which has infected more than 17,000 people— has disrupted world-wide trade and supply chains, depressed asset prices, and forced multinational businesses to make hard decisions with limited information.
The U.S., and governments in Europe and Asia are enforcing new regulations to block visitors from China and screen returning U.S. citizens, while major airlines suspended flights to the country and companies pulled out expatriate executives.
"The calls that I get are: 'We don't know what to do. Our employees are panicking,'" says Rachel Conn, an employment attorney in San Francisco at Nixon Peabody LLP. "They've never dealt with a situation like this."

Apple Inc. said this weekend it will close all of its stores and corporate offices in China through Feb. 9. The company, which employs 10,000 people in China, is also contending with work stoppages by factories that produce components for the products it sells around the world.
China's health crisis is testing the entire global economic system, and placing unexpected and additional strain on the fragility of an extended boom. It's also a test of China's strength as a consumer—and the U.S.'s ability to step up as China lags.
Levi Strauss & Co., which in October opened its biggest China store in the city of Wuhan, the center of the outbreak, is among the international brands that together have closed thousands of outlets around the country, including McDonald's Corp. and Starbucks Inc., in part to comply with government requests for people to remain off the streets.

Chinese factories that were supposed to be quiet for a few days to celebrate Lunar New Year are looking at possible closures and staff disruptions of weeks if not more, threatening production plans at Apple, as well as Tesla Inc. and Anheuser-Busch InBev SA .
Sagging demand for crude oil, which has stumbled 16% in price since China identified the coronavirus, is prompting Saudi Arabia, the de facto leader of the Organization of the Petroleum Exporting Countries, to push other members to convene an emergency meeting, OPEC officials said.

China is the world's biggest oil importer and the locked-down city of Wuhan, where the virus emerged, is one of its key oil and gas hubs. Two big Saudi customers, China National Chemical Corp. and Hengli Petrochemical —with refinery capacity of almost 1 million barrels a day—are reducing their purchases, according to an oil trader and a Persian Gulf oil official.
Beijing-based energy consultancy JLC Network Technology Co. reported a 15% drop in refinery use over the past week alone.

Chinese markets dropped sharply when they reopened Monday morning for the first time since Jan. 23, after the extended New Year break. The benchmark Shanghai Composite closed down 7.7%, wiping out nearly $400 billion in value. Retail, consumer services and transportation stocks led the declines. The Shenzhen Composite dropped 8.4%.

Coronavirus impact explained a lot of the 3.7% fall in the Dow Jones Industrial Average since it hit a record on Jan. 17, wiping out this year's gains.

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Pharmaceutical giants, financial institutions and technology multinationals are starting to evacuate their expatriate workforces from throughout China, according to Tammy Krings, chief executive of ATG Travel Worldwide who has dealt with "short and predictable" past natural disasters and terrorism scares. "This is just growing," she said.

Other companies are relocating staffers from China for three to six months. Some families are going so far as to seek new schools for their children— meaning they may be gone for good.

Boston Consulting Group has asked its staff in China to spend an extra week working at home after the holidays end and deferred all travel to mainland China for the next three weeks, according to a person familiar with the matter.

Air carriers including American Airlines Group Inc., Delta Air LinesInc. and United Airlines Holdings Inc. on Friday temporarily suspended flight service to China, as tourists canceled travel plans and crews balked at flying. Singapore said it will ban many visitors from China, while pressure builds on Hong Kong to seal its border with the mainland.

Since the virus first emerged in Wuhan, the biggest city in central China, in late December, it has killed more than 360 people, primarily in mainland China. The first—and so far only—death outside China was reported in the Philippines this weekend when the disease killed a 44-year-old Chinese man from Wuhan. So far, there are about 140 cases in 20 or so countries outside mainland China, including 11 in the U.S.

Many global companies are taking their cues from the World Health Organization, which last week declared the outbreak a public health emergency and said that many unknowns include severity, transmission and treatment of the novel coronavirus.
The virus appears to be less deadly than SARS, which killed about 10% of the people who caught it. So far, about 2% of the people infected with the new coronavirus have died. It is also much harder to transmit than the measles.

China's government reacted angrily to border restrictions and airline cancellations. "This kind of overreaction could only make things even worse," China's Foreign Ministry on Saturday wrote on its Twitteraccount. "It's not the right way to deal with the pandemic."
Speaking separately on Saturday as China's central bank and other agencies pledged support to the economy, a vice chairman of the China Banking and Insurance Regulatory Commission pointed to solid economic fundamentals in the country and predicted any market weakness would probably be "short-lived and temporary."

A decade and a half ago, when the severe acute respiratory syndrome outbreak known as SARS rattled the world, China accounted for a relatively small part of the global economy. Today, it is responsible for almost a fifth of global gross domestic product when adjusted for incomes—more than the U.S.'s 15% by the same measure, adding a morbid twist to the economic adage that when America sneezes, the world catches a cold.

China's heavily indebted economy has long been slowing. More recently, economists were rushing to boost predictions for Chinese growth this year on relief that Washington and Beijing had called a truce to their two-year trade war. Now the picture is changing rapidly as Chinese industrial activity and consumer spending slow.
Ten economists surveyed on Friday by The Wall Street Journal lowered their expectations for first quarter Chinese growth by over a percentage point to a median 4.9%. Those forecast cuts were made hours before the U.S. airline announcements.

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A likely fall in arrivals to the U.S. by Chinese—the globe's biggest-spending travelers—is one factor that could now dent first-quarter U.S. growth, economists said Friday.

The virus probably doesn't pose a serious threat to the U.S's decade-long expansion yet, they said. But that could change if the virus isn't contained soon, or spreads more widely.

Goldman Sachs on Friday said it expects the virus to reduce U.S. output by 0.4 percentage point to 0.5 percentage point, at an annual rate, in the first quarter, with growth rebounding in the second quarter, leaving minimal impact on full-year growth. Goldman projects U.S. output will expand 1.7%, at an annual rate, in January through March. Still, with news moving so quickly, no one really knows.

Ripple Effects

China's growing economic reach means the financial impact of novel coronavirus could be greater than SARS. A slowdown in consumer spending may reduce China's appetite for imports and a falloff in outbound travellers could depress tourist revenues

"It could be a few minimal tenths of a percent, or it could be up or near a full percent depending on the depth and duration of the actual exposure," said Lindsey Piegza, an economist at Stifel Nicolaus & Co. in New York.

The shock waves began Jan. 23, when Chinese President Xi Jinping ordered an indefinite transportation blockade around central Hubei province, an unconventional strategy to stop a virus originating in the province's capital, Wuhan. The lockdown covers a region of about 60 million, while other regulations nationwide are aimed at keeping people home.

Parts of the world are effectively seeking to quarantine China. On Friday, the U.S. government said non-Americans who had visited China will be quarantined 14 days upon arrival, in line with a WHO warning that the virus can linger undetected that long. The same applies to U.S. citizens who traveled in Hubei.
Several chief-executive letters to employees reviewed by The Wall Street Journal echoed the WHO concern by ordering travel restrictions to China. Consulting firms Ernst & Young and KPMG both went a step further, saying employees should stay home for several weeks after traveling to China.

The cutoff of flight service to China, by carriers from the U.K. to Singapore and Australia, appears unprecedented during peacetime—and possibly lengthy since Chinese health officials warn virus cases are still rising. A halt in 2010 to air travel over much of Europe after an eruption of Iceland's Eyjafjallajökull volcano lasted six days. Planes were back in American skies three days after the 2001 terrorist attacks, including over New York.

Forecasting the costs of the crisis is impossible. Last year, the WHO said in a report that it had tracked 1,483 epidemic events in 172 countries between 2011 and 2018. The most expensive in recent history include $40 billion in lost productivity due to SARS in 2003 and up to $55 billion during a 2009 H1N1 swine flu pandemic, both of which involved China. The WHO said an outbreak of Ebola in West Africa from 2014 to 2016 cost $53 billion in economic and social impacts.
When SARS hit, China's economy was on an upswing, with swelling numbers of outbound travelers and fast-growing trade, but it was only the sixth biggest economy, whereas today it is No. 2 in GDP and No. 1 in world trade. Only about 7 million ventured beyond Hong Kong in 2002, according to Goldman Sachs figures; the government now counts around 150 million international trips annually. Seven of the busiest 10 container ports are in China today, according to United Nations figures.

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During SARS, most Chinese factories and schools remained open, and the nation's contribution to global GDP was under half its value today, by the International Monetary Fund's measure of purchasing power parity.

Some past disasters, including floods in Thailand in 2011 and the earthquake and nuclear meltdown the same year in Fukushima, Japan, resulted in long-lasting changes to supply chains, even after immediate problems were fixed. Some international companies were already looking to relocate out of China before the virus outbreak, as tensions between Washington and Beijing have heated up in recent years and labor costs in China have risen.

It is uncertain when normal life will resume. Hundreds of millions of Chinese are currently reluctant to leave their homes, wiping out a traditionally important consumer boost during last month's Lunar New Year holiday. Fears are growing that companies already on the edge may have trouble surviving, especially if workers don't return, or the government sets new delays to business and school resumption.

The twin hits to businesses and consumers promise to at least temporarily reduce China's appetite for imports, despite its trade-deal pledge last month to boost by $200 billion purchases of U.S. goods and services over the next two years.

Costco Wholesale Corp., which last year opened a Shanghai outlet with much fanfare, says it could be three weeks before it can gauge any trade delays and import appetite since ships are already in transit.

"There are concerns about disruptions and what level of disruption and how long it is going to last," said Costco's chief financial officer, Richard Galanti. "There are a lot of unknowns."

One of the more bearish forecasts on China, from Chen Long of Beijing-based research firm Plenum, calls for growth to plunge to 2% in the current three months.

"The impact on the first quarter will be significant," said Mr. Chen, who bases his pessimism in part on an estimated 40% drop in Lunar New Year spending from last year. Holiday-related train and plane ridership was down 40% from the previous year, according to official data.

Chinese growth for 2020 as a whole was already widely forecast to slow further from last year's 6.1%, a three-decade low, with many analysts, speaking after the trade deal, predicting about 6%. Now, economists say those forecasts are optimistic.

Retail sales may now expand by only 3% to 4% in the first quarter from the same period a year ago, compared with 8% year-on-year growth in December, according to ING economist Iris Pang.

Joblessness and inflation could jump. Hubei is one of six central provinces that supply a third of the country's migrant labor to other parts of the country, and now many can't travel.

Huang Yiping, a former Chinese central bank adviser, warns that if just 5% of Chinese service-sector employees lose their jobs, that would mean 20 million out of work. Higher consumer prices would exacerbate already-elevated food inflation caused by a deadly swine fever, warns Zhang Ming, a researcher at the state think-tank Chinese Academy of Social Science. Adding to China's food supply challenges was a case reported on Sunday by its Ministry of Agriculture that an avian influenza, H5N1, had appeared in chickens Hunan province, compounding headaches for poultry producers near Wuhan who say transportation bottlenecks are leaving them short of feed-grain.

Mitigating some of the damage to China's economic figures is the fact that the first quarter of the year is typically China's least important economically, since the Lunar New Year holidays perennially result in factory shutdowns and slower trade.

Even with a disastrous first quarter, Plenum's Mr. Chen says that if the scare is short-lived, full-year growth could still hit 5.5%.

Furthermore, the coronavirus outbreak is primarily concentrated in Hubei province, which has expanded quickly as manufacturers move inland but is less than 4.5% of overall economic activity, and a similarly slight share of international trade and investment.

Goldman Sachs, while acknowledging uncertainty about the length of the epidemic, said that "past viral outbreaks have typically resulted in short, sharp shocks to economic output," lasting one to three months, with a return to past levels of activity within two or three quarters. That modeling, Goldman's economists said, would lower China's GDP growth for the year to 5.5%, down from their previous 5.9% forecast, while a more prolonged outbreak could mean a slump to 5% or lower.

After SARS, which took a heavy toll initially, China's economy still grew by 10% that year. The Tiananmen Square crackdown in 1989 dragged Chinese growth to 3.9% in 1990, though it was back to double-digit gains within two years of that slowdown.

But those were periods when China's economy typically grew much faster, with fewer ties to the global economy. Wuhan and the surrounding areas are vital parts of the global supply chain, and as long as they are walled off, that threatens supply chains producing products from automobiles to poultry.

Parts for iPhone maker Apple, including camera components, are made in Wuhan. .

"There are alternate sources, and we're obviously working on mitigation plans to make up any expected production loss," said Apple chief executive Tim Cook, who told investors Tuesday suppliers outside Wuhan were expected to reopen their factories by Feb. 10.

Measuring the macroeconomic impact hinges a great deal on disease control, and nobody knows when things will begin to return to normal.

"Things can turn positive over there just as quickly as they can turn negative," according to Patrick J. McHale, chief executive officer of Minneapolis industrial products maker Graco Inc. Still, he said by email his hope to visit Graco operations near Shanghai were upended Friday by the airline cancellations.

Yet another impact comes from the inevitable falloff in Chinese travelers. They represent 7% of all tourists to the U.S. and their spending is higher than any other foreign group at roughly $6,000 each for airfare, hotels, restaurants and shopping, according to research firm Tourism Economics. The firm expects 28% fewer Chinese visitors now, reducing spending $5.8 billion, especially in California and New York.

"If you're a hotelier in Los Angeles you're going to feel this," said the firm's president, Adam Sacks.

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