Do we see a recession for 2020?

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You've probably heard a lot of economists and strategists call for recessions, in Canada, the United States, or globally. A recession is essentially two back-to-back quarters of negative GDP growth. It's probably a little early to call for a Canadian or U.S. recession, although the likelihood of those is rising very quickly. Our concerns about growth come from three main issues. The first one is what we call the supply-side shock. The shutting down of China around COVID-19 and the challenge of bringing in intermediate goods from Asia to the rest of the world basically means that world trade and manufacturing will shudder almost completely, at least in February and March and possibly beyond. That effectively hampers or worsens the manufacturing recession that we experienced over the prior 18 months.

On top of that, we have to grapple with a demand-side shock, or a confidence shock. That is, everyday people, households, consumers and businesses now concerned about the future are less likely to spend. Some because they are scared, some because they are deliberately told they should not be going to work. That confidence shock is now going to hit the demand side of the economy, and consumption is likely to pull back. How long? Well, that depends on how long COVID-19 cases continue to grow. How long people are told to work from home. At least in our view, probably contributes to the second quarter or Q2 being a negative growth rate.

And then we have the third component of this story, which is a little bit darker, and that is what we are witnessing in funding channels. We're seeing a lot of tight credit. The credit market is increasingly concerned about the additional shock, falling oil prices, which is now creating some concerns that we might see company or corporate defaults start to rise. If that happens, then it does have some shades of a financial crisis, but we're not there yet. We have substantial central bank easing at play here, a lot of funding being provided through many central banks that are there to mitigate and learn from the lessons of 2008.

But as long as the market remains concerned that COVID-19, falling oil prices and defaults are a risk, we're likely to see the market in risk-off mode.

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