

MACROCOSM

Is Coronavirus a Chinese Bio-Weapon?

Monday, February 3, 2020

Donald Luskin

Definitely. Possibly. You can't rule it out. Well, not really. OK, it's a US bio-weapon.

It's been only a little more than a week since the outbreak of the temporarily named "2019-nCoV" coronavirus. Considering that it invokes memories of the 1918 "Spanish flu" pandemic (also possibly [of Chinese origin](#), despite the misnomer), in which [a third of the world's population was infected](#) and [as much as 5% of the world's population died](#) – and comes after a big bull run in equities – *it's amazing that the risk-off reaction has been so little other than in Chinese equities*. The S&P 500, as of this writing, is off 3.69% from recent all-time highs, and less than half a percent since coronavirus came into the headlines (please see the charts on the following page). *So our instinct is to expect at least as much of a risk-off correction as we had in 2003 with SARS – 6% in the S&P 500 – or in 2014 with Ebola – 10%* (see ["Another Damn Export from China"](#) January 27, 2020). *Yet at the same time, we're already seeing the signs of panicky crazy-talk that usually points to a bottom.*

- [An article](#) Friday in *The Lancet* featured a model predicting the spread of coronavirus "growing exponentially," and it has been cited in a number of [mainstream media](#) scare stories, with headlines like ["Coronavirus Explodes,"](#) or on the other extreme headlines about salvation by [drones spraying disinfectants](#). *The number of new daily cases made a new high yesterday after a flat week – that's not good, but it's not "exponential."* *Deaths are barely growing at all* (again, please see the charts on the following page). This reminds us of the climax of the 2014 Ebola panic (see ["Something You Probably Didn't Know about Ebola"](#) October 14, 2014).
 - *But the most chilling stories over the last week have been suggestions that 2019-nCoV is a biological weapon.*

CORONA BEER CHANGES THEIR NAME TO AVOID ASSOCIATION WITH THE CORONA VIRUS OUTBREAK



Update to strategic view

US MACRO, ASIA MACRO, US STOCKS, US BONDS, FEDERAL RESERVE, OIL, FX:

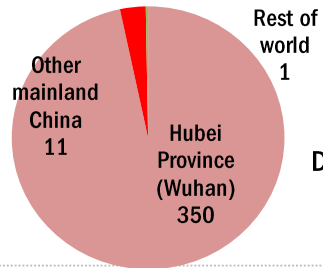
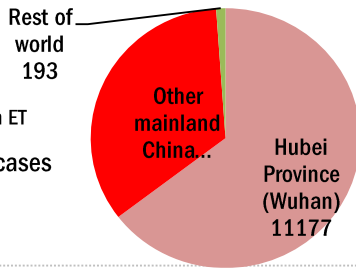
Considering the risks, asset markets have barely corrected in the face of the coronavirus outbreak. Yet already we're hearing the kind of crazy-talk that marks bottoms. Conspiracy theories are swirling that 2019-nCoV is a Chinese bioweapon escaped from a Wuhan level-4 lab. Indian scientists claim to have identified components of HIV in it, which are "unlikely to be fortuitous," but their paper has been withdrawn under criticism. Xi has put his reputation at stake on this, and is in "whatever it takes" mode in containment and financial support. OPEC and Russia are talking about supporting oil prices. US earnings upgrades are surging at rates not seen in a year and a half. The Fed has inverted the yield curve with its rate hike last week, but Powell is telling legislators he is ready to act. Asset markets were ripe for correction anyway, so we think there is likely at least a little more downside here. We are on the look-out for tape-bombs when companies start warning about earnings because of the virus, especially if they come when the statistics show the worst has already passed.

Left axis: — Daily reported cases — Daily reported deaths Right axis: key markets

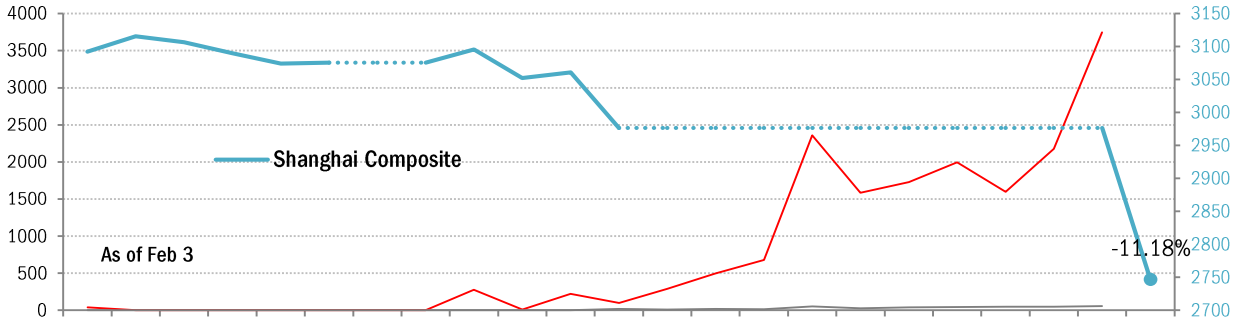
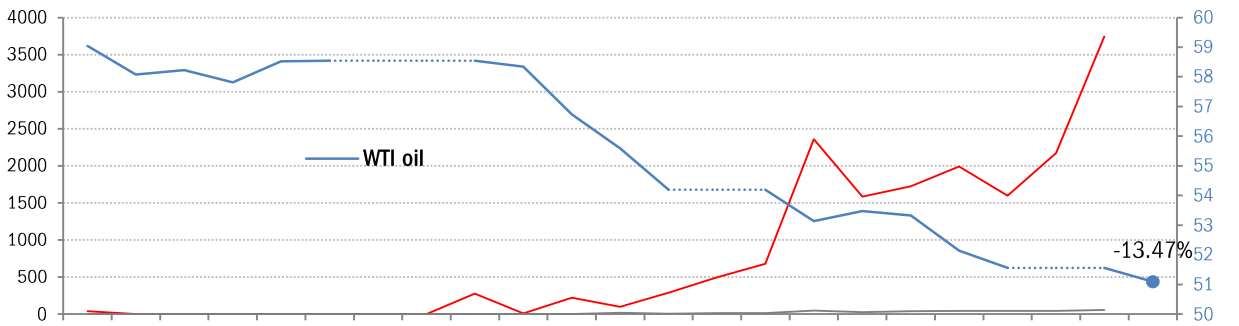
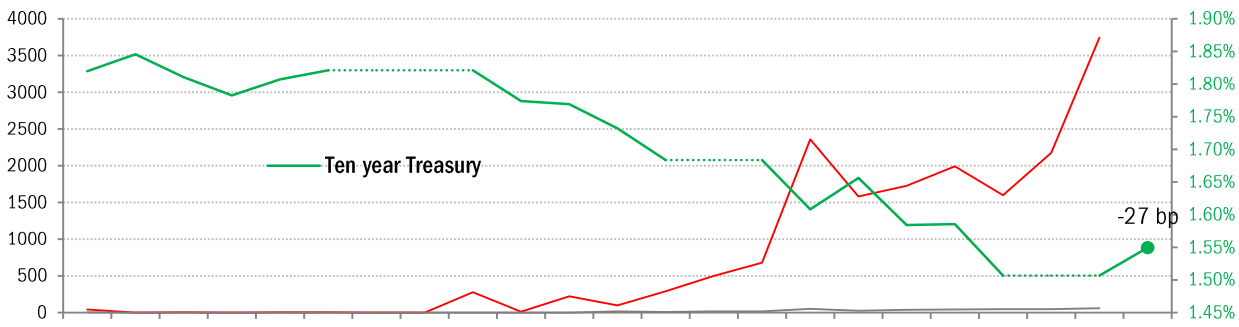
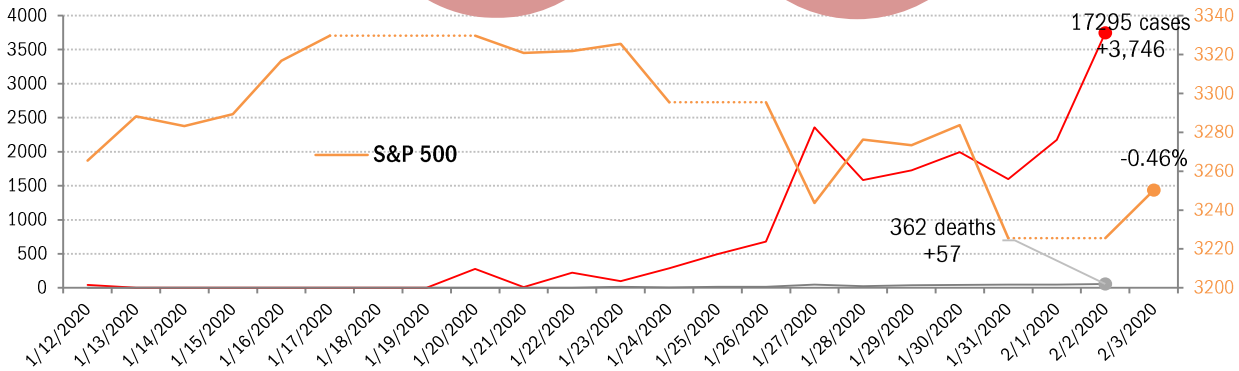
Virus stats
as of Feb 3

Markets
as of Feb 3, 9:38 am ET

Confirmed cases



Deaths



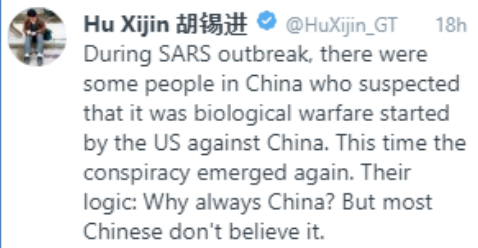
Source: Johns Hopkins, Bloomberg, TrendMacro calculations



- As far as we know, this thought contagion began on the Wall Street conspiracy-theory website Zero Hedge, which [ten days ago drew attention](#) to a Chinese [biosafety level-4](#) facility that researches and handles the most dangerous pathogens, and just happens to be located in – wait for it – Wuhan. It’s the Wuhan Institute of Virology, and it’s 16.6 miles as the crow flies, or 19.5 miles by car, from the Huanan Seafood Market where, many suspect, the coronavirus epidemic began.

- Zero Hedge last week ran an increasingly panicky series of articles on it, [including one “doxing” a particular researcher there](#) (naming him, and

publishing his email address and phone number), for which Zero Hedge was [permanently banned from Twitter](#). Zero Hedge’s target, one Dr. Peng Zhou, is an expert in the immunity of bats to coronaviruses, which makes them such good carriers. He is coauthor of [the paper two weeks ago](#) first disclosing the bat origin of 2019-nCoV. Zero Hedge’s conspiracy-theory is that Peng would be in an ideal position to weaponize a coronavirus, but this makes little sense unless it is a weapon to be used against bats. More likely Peng could help humans build bat-like immunities.



- The Chinese government was not pleased by these stories. It’s the kind of thing one can’t deny without dignifying it. So instead, China’s tweeter-in-chief Hu Xijin, the editor of the state-controlled *Global Times*, [suggested indirectly](#) that in fact it was a US bio-weapon.

- It all may seem far-fetched, but it is an astonishing coincidence that the biohazard facility is so close to the origin of the coronavirus. *And the implications of the idea that China would be developing such a bio-weapon – and that they would be so incompetent as to let it get out among their own population – is so chilling that we fielded a number of calls about it last week from very smart clients who were understandably concerned.*

- *We got quite concerned ourselves this weekend when a paper was published by a team of researchers in India claiming an “uncanny similarity” between the 2019-nCoV and HIV, the retrovirus underlying AIDS. The researchers wrote, “We found 4 insertions...not present in other coronaviruses. Importantly...all the 4 inserts have identity or similarity to those in the HIV-1 gp120 or HIV-1 Gag. ...4 unique inserts...is unlikely to be fortuitous in nature.”*

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[\[About us\]](#)

Recommended Reading

[Uncanny similarity of unique inserts in the 2019-nCoV spike protein to HIV-1 gp120 and Gag](#)

Prashant Pradhan, Ashutosh Kumar Pandey, Akhilesh Mishra, Parul Gupta, Praveen Kumar Tripathi, Manoj Balakrishnan Menon, James Gomes, Perumal Vivekanandan and Bishwajit Kundu
Indian Institute of Technology and University of Delhi
January 31, 2020

[Texas Is About to Go Blue! Never Mind](#)

Karl Rove
Wall Street Journal
January 30, 2019

[\[Reading home\]](#)

- *This would seem to offer a general path to the weaponization of a coronavirus not normally infectious to humans – meld it with another virus that is.*
- The paper was not peer-reviewed, and indeed is a “pre-print” – a publication directly by the authors of research that is still a work in progress. As it stands at the moment, dozens of comments appended to the paper on the [bioRxiv pre-print site](#) where it was posted have been harshly critical, accusing the scientists of being what Nassim Taleb would call “fooled by randomness.” and ignoring the genetic similarities between coronaviruses and AIDS so great that the former can be treated to some extent with medications designed for the latter, as was SARS. As of this writing, the paper has been officially withdrawn, and bioRxiv has posted a warning on its site about the preliminary nature of postings on 2019-nCoV.
- Even though it’s likely just a bogus conspiracy theory, the

plausibility to an alarming extent of the idea that 2019-nCoV is a Chinese bioweapon-gone-wrong speaks volumes about China’s present economic and geopolitical dilemma – it is increasingly being seen, both internally and externally, as too aggressive, too authoritarian and not quite competent. If global companies weren’t already concerned by their concentrated supply chain vulnerability in China, they sure are now.

- We used to joke that President Xi Jinping was

When Xi Jinping sneezes during the meeting



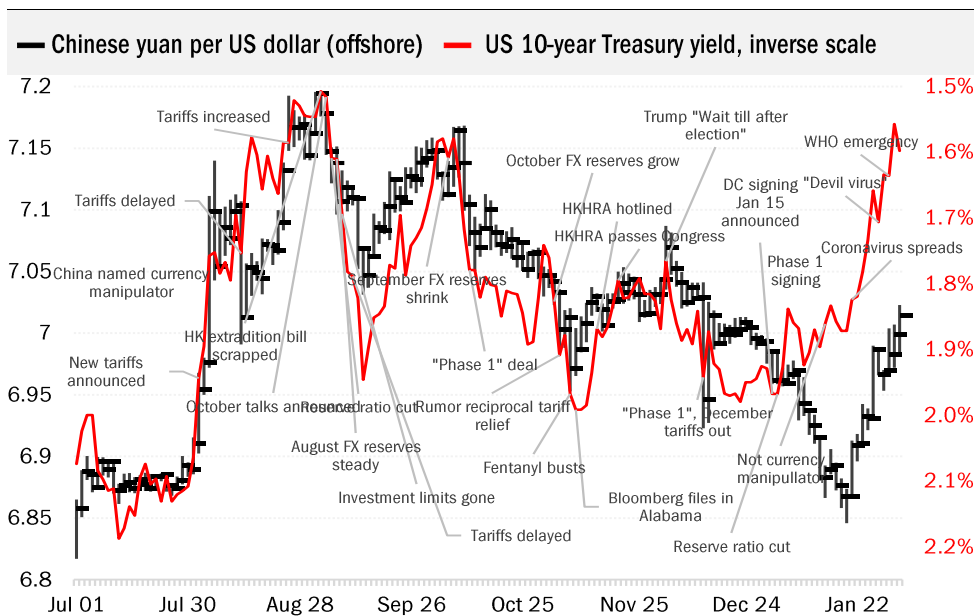
president for life only as long as he remains alive. At this point, having capitulated under duress to a US trade deal, suffering ongoing protests in Hong Kong, and now with the coronavirus – there’s a growing consensus that it’s [three strikes you’re out for Xi](#). If 2019-nCoV doesn’t kill him, the [long knives](#) will, some night.

- China has come under [severe criticism externally](#) – and even some gentle but atypical [criticism internally](#) – for initially hushing up the outbreak of the coronavirus with its typical penchant for secrecy and control, wasting precious days when it could have been studied and contained.
- Xi has now gone public with a very personal commitment to beating 2019-nCoV, calling it the “devil virus.”

He is probably unaware of the 1965 American movie called [“The Satan Bug”](#) in which a lethal virus escapes into the population from – wait for it – a government bioweapons lab.



- All that puts the Chinese government now in a position in which it is having to apply maximum force, whatever the cost, to contain the outbreak to both save lives and rescue its global reputation. That's all to the good, and we think markets are as relatively sanguine as they are precisely because of this "whatever it takes" approach.
- Locking down Wuhan and other cities is surely the most important step in halting the spread of the virus. The idea here seems to be for China to take a great economic hit – but take it quickly, and get it over with – so that it feels more like a temporary emergency than a recession. This feels like a risky "maximax" game-theoretic approach, but we think it's right in terms of managing business cycle dynamics in an economy that has never known a formal recession.
- But it's risky because how much hardship of this intensity the Chinese people can endure is unknown. There were riots under similar circumstances in 2003 during the SARS outbreak.
- At the same time, China appears committed to using all its financial tools to cushion the blow. Today [the PBOC announced a \\$21 billion monetary liquidity injection, and lowered rates.](#) And judging by how much the US 10-year Treasury yield has undershot the yuan/USD exchange rate, it would appear that the PBOC is doing its best – and for the moment only succeeding on an official basis – to support the Chinese currency at the psychologically important 7-to-the-dollar level again, while they had done nothing in August (please see the chart below, and "[Never Let a Good Currency Crisis Go to Waste](#)" August 14, 2019).

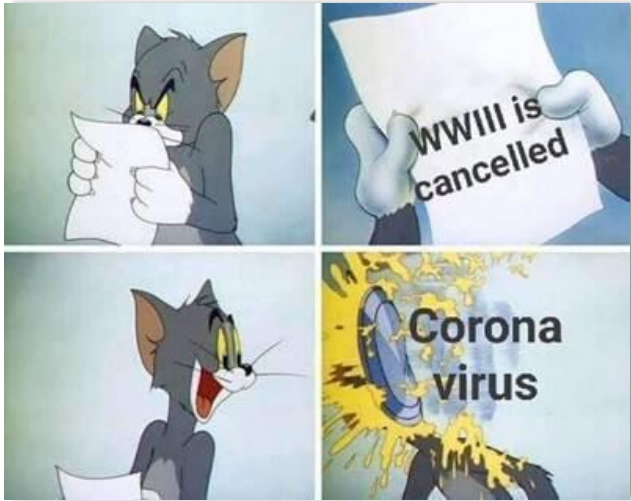


Source: Bloomberg, TrendMacro calculations

- At the moment our own Federal Reserve isn't playing along. The Fed subtly raised rates at the January FOMC, calling it a mere "technical adjustment," before the coronavirus matter reached quite the intensity of awareness it has today. That move has inverted the

yield curve, as we said it would (see [“On the January FOMC”](#) January 29, 2019). Now we are hearing that Powell is making the rounds on Capitol Hill assuring legislators that his central bank, like China’s will do whatever it takes if it comes to that. The PBOC’s actions today set the table.

- It’s also good news that OPEC and Russia are [openly talking about emergency production cuts](#) – with [Saudi Arabia alone talking](#) about cutting 1 million barrels per day – to support the oil price in the face of a temporary deep dent in Chinese demand ([panicky stories](#) are circulating this morning that Chinese demand has already fallen 3 million barrels, which we be about 20%). For the global economy, production cuts are as important as anything China might do for its domestic economy. *A collapsing oil price, and the knock-on fall in inflation expectations, rising real rates and widening credit spreads is one of the most dangerous vectors for economic contagion,* and OPEC production cuts are the only possible solution (see [“After Soleimani, What If Peace Breaks Out All Over?”](#) January 6, 2020, and again [“Another Damn Export from China”](#) January 27, 2020).
- Also on the good side is the excellent US earnings season that’s wrapping up now with a 5.4% upside surprise factor, and a one-year-forward upgrade rate surging above 10% per annum, a growth rate not seen in a year and a half. *It’s bearing out our view that there was a near-miss recession in 2018-19, and we’re now beginning to sling-shot out of it* (see [“2020 Outlook: After a Near-Miss Recession, It’s the Election”](#) January 2, 2020).
- There are now an increasing number of [mainstream stories](#) about the risk to the global economy arising from the coronavirus, so that’s no secret. There are some company-specific stories, such as Apple [fretting about its supply chain](#); and [Apple and Starbucks closing their stores](#) in China. *What worries us is the tape-bomb risk when that day comes that a slew of companies suddenly guide earnings down because of it. We may see a bottom if those announcements come when the virus-tracking statistics show the worst has already passed.*
- *Another element is the risk to the US election.* As always, please understand that as we talk about politics, we are speaking only about its effect on the economy. In this case, our worry has been that an economic downturn triggered by the coronavirus would trigger a vicious cycle in which markets would fear that President Donald J. Trump could not get elected in a weak economy, with those very fears making the economy weaker still (again, see [“Another Damn Export from China”](#) January 27, 2020).
- At the moment, the dynamics of the US presidential election are shaping up well – though the virus hasn’t been a factor yet. With the impeachment fiasco wrapping up unsuccessfully for the Democrats, it seems that Trump’s most fervent opponents among voters are mobilizing behind Bernie Sanders (D-VT) as today’s Iowa caucuses bring the election into real focus. Sanders is a radical alternative who is likely unelectable. *Whatever one may think of Trump personally, we have deep conviction that reversing his tax cuts (particularly on corporations) and reversing his pro-business stance (particularly on fracking) would be catastrophic, so*



the emergence of an unelectable opponent is all to the good for markets (see [“2020 Outlook: After a Near-Miss Recession, It’s the Election”](#)).

- So too bad about the global pandemic thing. Just when everything was going so well.

- We continue to fear we don’t get out of this so easily, especially when asset markets were ripe for correction anyway. But we’re starting from a

position of strength, and the relevant authorities are in whatever-it-takes mode, or getting there. With all the crazy-talk in the air, maybe we’re near the end of the beginning of the end (if you know what we mean).

Bottom line

Considering the risks, asset markets have barely corrected in the face of the coronavirus outbreak. Yet already we’re hearing the kind of crazy-talk that marks bottoms. Conspiracy theories are swirling that 2019-nCoV is a Chinese bioweapon escaped from a Wuhan level-4 lab. Indian scientists claim to have identified components of HIV in it, which are “unlikely to be fortuitous,” but their paper has been withdrawn under criticism. Xi has put his reputation at stake on this, and is in “whatever it takes” mode in containment and financial support. OPEC and Russia are talking about supporting oil prices. US earnings upgrades are surging at rates not seen in a year and a half. The Fed has inverted the yield curve with its rate hike last week, but Powell is telling legislators he is ready to act. Asset markets were ripe for correction anyway, so we think there is likely at least a little more downside here. We are on the look-out for tape-bombs when companies start warning about earnings because of the virus, especially if they come when the statistics show the worst has already passed. ▶