Markets in a Minute

7 July 2020

Markets shrug off virus concerns

Shares head up despite surge in cases

Most share markets rose last week although Britain's FTSE100 was flat, weighed by a poor session last Friday due to fears about the intensifying Covid crisis in the US. The same concerns also led to losses across Europe on Friday.

On Monday, however, the bullish mood returned following big gains in Asia where shares in China jumped by a whopping 5.7% due to renewed optimism about the country's continuing economic recovery and apparent success in containing the virus.

Western markets followed suit with healthy gains, ignoring the continued dreadful Covid statistics from the US over the weekend.

In London, the FTSE100 rose by 2.1% on Monday. European markets were all up by more than 1.5% and in the US, the S&P500 rose by 1.6%, but the tech-heavy Nasdaq rose by 2.2% to close at a new all-time high.

Last week's markets performance*

- FTSE100: -0.03%
- Dow Jones: 3.25%
- S&P500: 4%
- Dax: 5.56%
- Nikkei: -0.1%
- Hang Seng: 3.35%
- Shanghai Composite: 12.5%**

** Data for the week to close of business on Friday 3 July*

***Data for the week to close of business on Monday 6 July*

The US battle with coronavirus

It has been a mixed week for news about the spread of coronavirus. Earlier in the week the growth rate of cases in the US had been slowing, only to pick up again.

Clearly, the best outcome for the economy would have been for the southern (and western) US states to reopen their economies without cases rising. Sadly, that does not appear to be the case.

The next best news for the economy would be the US states being able to reopen without requiring lockdowns. That is the path that the states are trying to tread at the moment. So far, they are struggling. Baby steps are being taken to try and limit the spread, such as the closure of bars (which is economically disruptive) and the mandated wearing of masks (which is not).

> *"In summary we should be surprised neither by the speed of the initial rebound, nor a subsequent tapering of that recovery."*

Markets remain positive

The market stumbled with news of the restrictions last week, but now it seems to have found peace with the idea. Although as we head into the summer months, when lighter trading volumes tend to lead to more volatile markets, there is clearly more scope for wild swings.

Further lockdown measures may yet be required. But there is also the possibility of positive surprises. For example, we expect that the mortality rate will be lower as cases are limited largely to the young who are more resilient to the virus.

Although there has been the odd weak day for equities, the general direction of stock indices has been up, despite a change for the worse from Covid cases numbers. Naturally this means the market is vulnerable to a short-term pull back if investors begin to take a glass-half-empty view of the situation as opposed to the overwhelming optimism that has dominated sentiment so far.

Policymakers to the rescue

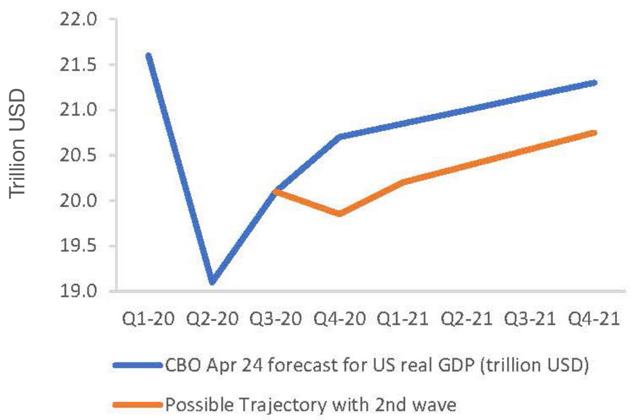
It seems that investors are taking the view that if the virus does come back then, even though there may be economic disruption, it will be met by powerful monetary easing. In the new world of enlightened Keynesian policymakers that might be associated with added fiscal stimulus as well, but it is the implied liquidity injections and focus on financial conditions that lure investors back into the water, and that is likely to continue.

The challenges ahead

The Bank of England's chief economist Andy Haldane voted against the added £100bn of QE announced by the Bank last month, arguing that signs so far suggest the recovery is "V-shaped." His colleagues on the Monetary Policy Committee and the IMF's Chief Economist Gita Gopinath warned the Treasury Select Committee that after an initial spike "we could end up with something much more flat", which chimes with our view.

In summary we should be surprised neither by the speed of the initial rebound, nor a subsequent tapering of that recovery.

The shape of the recovery



Source: Datastream July 2020

Fiscal support

It will therefore be interesting to hear what Rishi Sunak announces in tomorrow's mini budget because an early withdrawal of fiscal stimulus is probably the next risk the economy could face as finance ministers need to start counting the cost of their support programs.

In the US, too, there is a risk that policy could be constrained based upon strong headline economic data. Strong jobs growth in the nonfarm payroll report may discourage Congress from further fiscal support but the numbers merely reflect those on temporary layoff returning to work, while beneath the surface, the more serious non-temporary layoffs continue to rise and re-employment opportunities will be few. All of which should strengthen the case for continued fiscal stimulus, a major part of which – the extra $600 a week in unemployment benefits paid to those who lost their jobs due to the coronavirus – is due to expire at the end of the month. Democrats are calling for the payments to be extended and based on recent performance, the market appears to be pricing in an extension as well.