Boom Boom Boom

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June 23rd 2020

"Boom Boom Boom" is a 1995 song by the American hip house duo 'The Outhere Brothers' from their debut album. The title certainly inspired the punters as it topped the charts in Germany and the United Kingdom and was a top 10 hit in 11 European Countries. Markets right now are a lot more Boom Boom Boom than post pandemic hell! So it makes sense to analyse the recent market developments that have clearly inspired many investors.

Are punters merely dining out on adrenalin, praying that hope will continue to spring eternal, or is there something more substantial going on? At 1.30pm BST on Friday June 6th, the official US payroll data posted saw a positive number of 2.5m jobs created versus a -7.5m estimate. Yes, a massive negative expectation which itself was an improvement on the staggering negative -20.7m in April. What emerged was a US unemployment rate of 13.3% versus 19.0% expected and 14.7% in April. In a heartbeat, the DJIA futures rose like the proverbial grilse adding 750 points closing at 27110.

There were other factors that have contributed to this rally which indicate a 'V' shaped recovery is a possibility. American factory activity rose from April's 11 year low, with the ISM manufacturing index edging up to 43.1 in May from 41.5. Here in Old Blighty, the PMI index, compiled from surveys of business activity – rose to 40.7 in May from 32.6 a month earlier. European figures showed a similar trend.

As a result we have dusted off our bullish scenario for further upside if economic normalization continues. For such a scenario we have to assume governments in major economies will not need to reimpose lockdowns and the exceptionally loose monetary policy will continue for the foreseeable future.

The key drivers are:

- Additional stimulus: The ECB this week added EUR 600bn to its bond purchase program while Germany unveiled a new fiscal package worth EUR 130bn. This leaves the ECB on track to purchase EUR 1.4tr of assets this year. Meanwhile, the combined US fiscal and monetary stimulus is worth more than 50% of US GDP by the end of 2021.

- Increases in mobility: There have also been encouraging signs of normalization in travel patterns. American Airlines announced that it plans to fly 55% of its regular domestic schedule in July, up sharply from just 20% in May.
- Lack of new virus cases: Despite the rebound in mobility, so far we have seen no acceleration of infection rates in nations such as Germany that were among the first to end lockdowns. This should increase the likelihood that lockdown measures will continue to be eased in the coming weeks, allowing a sustained recovery to get underway faster.

We still expect some restrictions on public gatherings and international travel to remain in place until the end of 2020. Our best guess for large-scale production of a vaccine is Q1 2021, but there are promising headlines around this. What is essential for our bullish scenario to become a reality is any recurrences of the virus are accommodated by healthcare systems and lockdowns are not re-imposed. This would allow a sustained economic recovery to begin from 3Q20, and social activity to return to pre-pandemic levels in 1H21. For this scenario to occur we will need to see, a rollout of test and trace models, increased ICU capacity, and use of antivirals to help healthcare systems cope with demand.

Like the markets we believe that this is all possible and things are moving very quickly. In any case it’s a relief to have some good news to cheer our battered souls!

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