Quarterly Market Outlook

November 2020

The Economic Recovery Slows

As the global economy gradually recovers from the pandemic, the pace of improvement has slowed after an initial snap-back. Recent weeks have seen initial unemployment claims stabilizing around 800,000 per week, well above the pre-crisis levels of 200,000 per week.[1]

The Pandemic Continues to Disrupt Western Economies

The US faces renewed economic headwinds with a surge of new confirmed cases of COVID-19 during the third quarter (driven by increases in the southern states), with the 7-day average peaking near 70,000 daily during July.[2] Europe has experienced a similar resurgence in recent months, reaching approximately 50,000 daily cases at the end of September.[3]

Political Polarization is a Roadblock

With monetary policy limited by zero interest rates, additional stimulus depends on fiscal authorities working with central banks to spend the money that is printed. This unique dynamic presents new complications and potential delays relative to typical central bank driven monetary easing. As an example, Congress has not been able to agree on a second major stimulus package following the CARES Act enacted in March. This leaves many Americans short on funds.

Equity Markets Stage an Impressive Run

Equity markets extended the rally during the third quarter with global equities (MSCI ACWI) delivering a quarterly return of 8%, fully retracing the losses from earlier in the year (up 1% on the year). The S&P 500, due to its higher technology weighting, reached an all-time high in early September and finished the quarter up 6% on the year.[4] We believe the market response is being driven more by extraordinary monetary and government support rather than vastly improving economic fundamentals.

The Fed Changes its Mandate

In another sign of a mindset shift, the Federal Reserve announced an "average inflation targeting" policy, under which they will seek to exceed the 2% annual inflation target for some period of time to make up for years below the 2% target. This was viewed as a dovish stance, and markets now expect short rates to remain at zero through the end of 2023.[5]

Inflation is Far from a Certainty

While the focus has swung from fighting to generating inflation, it is noteworthy that Europe and Japan have been unsuccessfully trying to increase inflation for over a decade. This reflects ongoing major global deflationary forces (high debt, aging demographics, technological advances) that may be difficult to overcome.

[1] Source: U.S. Department of Labor
[2] Source: Johns Hopkins Coronavirus Resource Center. https://coronavirus.jhu.edu/data/new-cases
[3] Source: Politico. https://www.politico.eu/article/coronavirus-in-europe-by-the-numbers/
[4] Source: Bloomberg
[5] Source: Bloomberg

Presidential Election Takes Center Stage

Betting markets appear to favor a Biden victory in November (or whenever the results are finalized). This may be negative for growth from a tax perspective but would be offset by potential fiscal spending (additional stimulus, infrastructure spending, etc.), which could be larger in the case of a Democratic sweep. While markets are expecting heightened volatility around the election, we do not anticipate a contested election to have a long-term impact to asset markets.

Diversification is Critical

Facing an ongoing pandemic, exploding debt levels, and increasing political uncertainty, we expect a wide range of potential outcomes for markets, with large dispersion across economies and sectors. We could experience anything between outright deflation (like the 1930s or Japan since the 1990s) and high inflation (like the 1970s). Nominal growth may continue to rebound strongly, or we could face a prolonged period of economic weakness (or somewhere in between). Given these conditions, we strongly urge investors to maintain a well diversified portfolio.

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