Weekly Market Summary

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Market Uncertainties and Financial Bubbles Keep Growing … Central Bankers Nowhere in Sight!!

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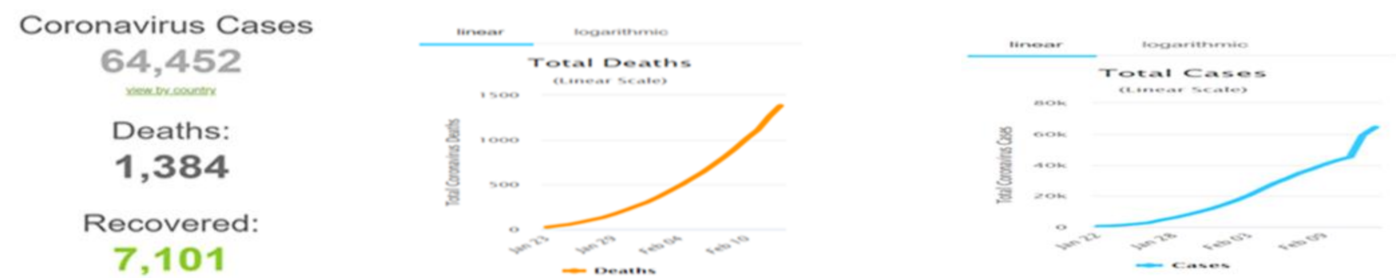
Latest Update on Coronavirus: Confirmed cases last at 64,452 (versus 31,477 last Friday), 1,384 deaths (versus 638). Hundreds of Chinese frontline medics likely infected with the virus. At least 25 countries with confirmed cases, three deaths so far being recorded outside mainland China. Passengers on the MS Westerdam cruise ship, previously turned away from ports around Asia over fears they could be carrying the new coronavirus, finally begin disembarking in Cambodia today. And last Tuesday, the International Committee on Taxonomy of Viruses officially named the coronavirus-associated disease "COVID-19"!



Economic recessions are periods of general economic decline (a technical recession being defined as two consecutive quarters of negative growth) that are typically accompanied by a sharp fall in equity prices, a loss in jobs, a drop in consumer and business confidence and a decline in the housing market. The blame for a recession generally falls on the political or monetary leadership (either the President himself, the head of the Federal Reserve or the entire administration), and is too often the result of fiscal or monetary errors such as elevated interest rates, fiscal tightening, inflated local currency, significant social inequality/imbalances and reduced wages. Still, at times, the responsibility may solely fall on exogenous factors and external shocks (coronavirus and middle east tensions come to mind!). So far, the US has experienced 33 recessions since 1857 according to the NBER (National Bureau of Economic Research), varying in length from six months (January to July 1980), to 65 months (October 1873 to March 1879). The average contraction lasts 17.5 months, but since 1945 durations have shortened significantly, averaging a bit less than a year. These shorter downturns are usually referred to as V-Shaped recessions; in this scenario, an economy deteriorates sharply but then quickly recovers ("sharp and quick"). In contrast, during a U-shaped recession, the economy takes a much longer period of time to recover (usually in the neighbourhood of 18-24 months, "long and protracted" a la 2007 -2009 economic slump). More importantly, recessions aren't always so bad! Yes, they do result in a rising number of unemployed, lower asset prices and higher business /consumer anxiety, but they also lead to a positive change in consumer attitudes (refrain from living above your means), a removal of excesses out of the economy (preventing asset bubbles from further growing and zombie firms/investors from persisting) and a better balancing of economic growth (higher national savings rate and improved investment opportunities).

Over past years, we have often referred to President Trump's growing influence on financial markets with his Twitter account becoming a primary source of market movements and heightened asset volatility (Check "*Goodbye Fed Watchers … Hello Presidential Tweet Followers !!*" - March 2018 on www.gib.com website > Treasury > Market Updates). In fact, the US President tweets became so consequential to many investors - especially fixed-income and equity traders, that it prompted analysts at JP Morgan to create the "*Volfefe Index*" (a combination of the word "volatility" and the infamous Trump "Covfefe" tweet) which quantifies Treasury yields movement in the five minutes after a Trump tweet and then shows the rolling one-month sum of inferred probability. JP Morgan analysts found that their newly coined index is able to account for a "*measurable fraction*" of moves in rate implied volatility, mostly apparent at the shorter end of the curve (two- and five-year yields). Lately, however, market attention has fully shifted to more relevant daily updates relating to the death / infected patients' tally from the coronavirus; Take for example Tuesday night's notice, which showed China reporting its lowest number of daily new coronavirus cases since late January as well as a reduced one-day increase in the death toll. Markets reacted quickly, with shares rallying in Europe and the US (to new record highs there!), whilst government bond markets sold-off and yields jumped. Nonetheless, the move was short lived and by late evening had started reversing on news that total infection cases in China had jumped by almost 15,000 (for Wednesday alone) while the death toll had risen by a daily record of 254!

Wait a minute! There is always a logical explanation to everything: Those latest large increases were simply the result of the Hubei province, the epicentre of the coronavirus outbreak, revising its method for counting infections after two top officials were removed in the biggest political fallout so far from the epidemic (not to mention a top WHO official confirming that many of the added cases dated back days and weeks! Seriously?). Still, surely a newly adopted and more transparent methodology would not justify a larger jump in the death toll! Or maybe it can! It turns out that the death figure on that day was prone for a downward revision (from 254 to 146), as some initial 108 cases were previously included due to double-counting in the Hubei province! ☺ And whilst the Trump administration has started raising doubts about the accuracy of data coming from China on the coronavirus (While House senior economic adviser Larry Kudlow stating overnight that the US is a little dismayed with China's lack of transparency over latest outbreak), the US President continues to praise China – mostly its leader Xi Jinping – for the Asian giant's efforts in containing the spread, while also suggesting that he expects the virus outbreak to disappear in April due to hotter weather (such statement surely gathers more credibility coming from an anti-climate, anti-public health champion! ☺)

The matter of the fact is that the coronavirus complacency has surely arrived ahead of schedule! Scientific models still show a reasonably high probability that the Wuhan virus will accelerate in its spread outside of China at a time the tone of news coverage is swinging the wrong way, offering too much false reassurance. Whilst that would not impose an immediate threat to most people's lives, the disease could still easily disrupt business and everyday life for millions of people. Wednesday's cancellation of the MWC Barcelona 2020 exhibition (which was supposed to run from 24th to 27th February and draw more than 100,000 people to the Spanish city), the wireless telecom's top annual event, after several large phone carriers opted to pull out because of concerns about the spread of the virus is a clear example of global economic disruptions. Add to that Alibaba Group's latest adverse projections: The Chinese e-commerce giant warned yesterday that the coronavirus is exerting a fundamental impact on the country's consumers and merchants, and will hurt its revenue growth in the current quarter. Alibaba, the first major Chinese technology corporation to report results since the epidemic emerged in January, added that the virus is undermining production because many workers cannot get to or perform their jobs. It has also changed buying patterns with consumers pulling back on discretionary spending, including travel and restaurants. The company's U.S.-listed shares closed 1.8% lower yesterday.

It appears that few economists are now starting to turn more pessimistic over the chances of a speedy recovery (V-shaped) as evidence mounts that the disruption will be deeper and more long-lasting than first thought and as factories and business struggle to re-open amid curbs on movement. Chinese officials continue to assume that government stimulus, though moderate, will help cushion a large part of the blow whilst the PBoC (China's central bank) mulls further liquidity injections and more rates trimming to support markets. Also global policy makers remain on the alert for a longer slump with US Federal Reserve Chairman Jerome Powell singling out the virus among the risks to U.S. growth. "*In particular, we are closely monitoring the emergence of the coronavirus, which could lead to disruptions in China that spill over to the rest of the global economy*," Powell said in remarks before U.S. lawmakers earlier this week. Nonetheless, Powell stopped short of saying the outbreak had changed the Fed's baseline outlook for the U.S. economy, or the expectation among many members of the Federal Open Market Committee that rates will remain on hold this year. "*The FOMC believes that the current stance of monetary policy will support continued economic growth, a strong labour market and inflation returning to the committee's symmetric 2% objective,*" Powell noted. "*As long as incoming information about the economy remains broadly consistent with this outlook, the current stance of monetary policy will likely remain appropriate*."

In other major news, the Covid-19 outbreak has polished the USD's appeal as a high-yielding safe-haven currency. Specifically, the global health scare has further deepened the perceived growth outlook divide between the US and the Eurozone as robust domestic demand in the US helps shield the economy, whilst the Eurozone's heavy reliance on global trade exposes its economy to renewed growth headwinds from China (EUR/USD last trading at 1.0835, down from 1.1225 as of December-end 2019).

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