Market Flash – 7 April 2020

What happened?

- Better news about a likely peak in cases in many European countries and even New York propelled stocks higher yesterday, with the S&P500 up 7% to its highest level since 13 March and the Stoxx50 up 5%. Coupled with headlines that oil production may be cut, markets found some much-needed support. However, volumes were still relatively low, gold was up throughout the day, rising to USD1680 per ounce before retreating to USD1662 per ounce this morning, and the VIX volatility index was flat around 45, indicating that concerns remain. This morning, futures are still pointing up.
- Sovereigns yields rose as a result, with the US 10-year yield climbing to 0.71% and the German 10-year Bund rising to -0.42%. Credit spreads tightened across segments, with IG down about 9bp in the US and 3bp in Europe, while HY was down 16bp in the US and 11bp in Europe. And funding markets are showing signs of stabilisation as well.
- Oil gained a few more dollars as talks continue between major producers about possible cuts, pushing Brent to USD34 per barrel and WTI to USD27 per barrel. In our view, even if OPEC+ does cut production, the current collapse in global demand suggest limited upside for prices in the short term.
- In our view, markets are likely still underestimating how long containment measures will last, and particularly how long it will take to get back to 'normal' afterwards. As we see better news about 'peaks' across many regions, we could see optimism in markets, but the reality that economic activity will ramp up slower than anticipated, and even worse than expected data releases could hurt sentiment again. Indeed, while we continue to believe that a peak in cases will likely be needed for a sustainable recovery, questions about the recovery are just beginning.
- We do not expect a V-shaped rebound, but rather a U-like shape, but with only a gradual way up (not vertical). With staggered progress in the fight against the outbreak, staggered responses and different levels of containment, we are unlikely to see a general 'all clear' and a resumption in activity. It too will be staggered between regions, countries, US states and industries, suggesting a slower ramp up than originally hoped for. As such, we believe that high volatility and downside risks will remain for some time.

What we are watching

- We continue to monitor plateauing and peaking cases in countries more 'advanced' in the outbreak for signs of how long stringent containment will be necessary. The longer the economic standstill lasts, the bigger the damage and the higher the risk of negative consequences.
- We look at how stimulus can be deployed to avoid waves of bankruptcies and defaults, and at how defaults can be ring-fenced if/when they happen.
- We keep an eye on credit and funding markets to see if massive central bank measures, both in the US and Europe, help ease the recent stress. For now, we believe that central banks will succeed in keeping systemic risks low to prevent a credit crisis.

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