



Institutions are deploying their full arsenal to contain the crisis

While more than 2.5 billion people worldwide are currently confined to their homes, the situation on the financial markets remains conditioned by the evolution of the pandemic. After a clear improvement in Asia, attention is now turning to Europe where some observers agree that we could reach the peak of the contamination very soon, even if, for the time being, the data remain unreliable as the number of cases depends on the number of people tested.

The United States are now the main concern, following the statement by President Trump who tried to adopt the strategy that Boris Johnson had to abandon in the United Kingdom, where there is uncertainty about the real impact of COVID-19 on the economy if containment were not widespread. However, and in spite of these elements, the equity markets, after rebounding by about 15% from the low of March 16, seem to be back to their average level of the last ten days and mark a halt in this fall in view of a number of more favourable elements.

First of all, the stimuli put in place by various authorities, first and foremost the intervention of the monetary authorities, recalling Mario Draghi's formula "Whatever it takes". Indeed, all the Central banks have provided the financial system with almost unlimited facilities to meet financing needs. These measures represent more than 750 billion euros released by the ECB in the Eurozone, in addition to the 120 billion already mentioned, while in the United States the Fed has announced an unlimited capacity to purchase bonds or mortgage and commercial securities. These measures provide the necessary financing for the gigantic credit facilities granted to companies.

In addition to this monetary stimulus, there is also a fiscal stimulus, which could be called "Whatever it costs" to use the terminology used by President Macron, on a massive scale in the United States with more than USD 1,100 billion, nearly 5.4% of GDP, of which USD 500 billion is paid directly to American households. In the euro area, budget spending announced to stem the recessive effect of the crisis represents around 2.5% of European GDP, with Germany contributing nearly half of this through a €156 billion (4.5% of GDP) recovery plan. This does not include the guarantees provided by the States, which represent 24% of GDP in Germany, 12% in France and 20% in Italy.

We will also stress that the euro crisis, which occurred in 2011-2012, have had the positive consequence of providing the ECB with tools, such as the ESM⁽¹⁾ and the OMT⁽²⁾, in a context where, for the moment, the German, Dutch and Austrian governments refuse to commit themselves further to monetary union by issuing eurobonds, renamed "corona bonds" in the current circumstances. A solution that the French Presidency and eight other European leaders have called for and which might have the effect of demonstrating solidarity within the Union but also putting an end to the controversy over monetary integration in the Eurozone.

Governments and monetary institutions therefore decided to use a double "bazooka", through larger measures than those put in place in 2008, but commensurate with the unprecedented economic shock confronting the world economy. These interventions had the effect of reassuring the markets and providing the necessary liquidity to certain investors who could fear a liquidity crisis, prompting them to sell at all costs. Furthermore, short-term investors, like hedge funds or quantitative and systematic strategies, early cut their positions, deflated their balance sheets and lowered their gross exposure, with the effect of clean up the markets. In addition, some asset managers, in order to maintain an exposure in line with their objectives had to reinvest after the equity proportion in their portfolios was diluted as prices fell.



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(1) European Stability Mechanism
(2) Outright Monetary Transactions

A recession in 2020 seems inevitable, although its full extent is not clear yet, economists have begun to factor a decline in activity of around 3% to 5% for the Eurozone, more limited in the United States at this stage. Strategists are expecting earnings declines between 20% and 30%. These figures coincide with the downturn generally observed during a recession and usually leads to equivalent declines in equity markets. The key issue now is whether the measures implemented will be effective in enabling a significant rebound in growth and earnings for 2021. The estimates mentioned above correspond to a widely held opinion, supported by the measures introduced by the authorities. However, some are more pessimistic and consider that the shock to the production capacities apparatus could lead to a weak rebound in activity, or even a depression.

We belong to the first category and are trying to identify assets that, following this unprecedented correction, show attractive levels of risk premium. These include some cyclical and oil stocks that have posted declines of more than 50% within a month, as well as a few stocks in a credit market where non-investment grade bonds have seen their yields rise by an average of 400 to 500 basis points over the same period. Bear in mind that, due to the mid-March correction in the equity markets, the global index⁽³⁾ excluding the US and excluding dividends is back to the levels it had reached in March 1997 and September 2008.

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(3) MSCI World

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