Letter n°30

What to make of the ambivalence of the crisis and the intermittency of the recovery?

An atypical crisis and an intermittent recovery for the time being. A strong recovery with each deconfinement but is frequently interrupted, it restarts rich in hopes but is sowed with disillusionment. And as ***Charles Baudelaire*** wrote in his poem Elevation ***"Behind this boredom and fatigue, this vast chagrin/ Whose weight moves the mists of existence, / Happy is he who vigorously fans the senses / Toward serene and luminous fields – wincing!"***

To understand the magnitude of the crisis in 2020, let us look at one figure – the decline in world GDP. The figure stood at $3 trillion, which is roughly equivalent to Germany's annual GDP and, according to the IMF, should there had not been a crisis, global GDP by the end of 2021 would be $12 trillion higher than what it will be.

In order to better understand the ambivalence of this crisis, we will analyze 9 surprising developments:

An atypical crisis at the budgetary level: on average, in developed countries, from the United States to Japan and including Europe, budget deficits have reached 12% of GDP, a level incomparably higher than the 8% recorded in 2009, or the 4% deficit in the aftermath of the 2001 crisis.

In other words, never before have governments spent so much to pull their economies out of the crisis and to get them back on the path of growth quickly. The best example of this cultural revolution in the use of the budget deficit is Germany: in 2008-09, the budget deficit did not exceed 3.3% of GDP, in 2020 it has reached 9.5% of GDP. Orthodoxy has been forgotten.

An atypical crisis in terms of investment as the global decline was moderate. The cyclicality of investment compared to previous crises has been much lower. The inevitable contraction in the second quarter of 2020 was followed by a recovery beginning in the third or fourth quarter.

This has nothing to do with the 1929 crisis or other crises because the guarantees provided by central banks or governments for corporate debts served as a buffer.

Today, the PMI indicators are very high and order books are improving. In February this year, industrial production in China and India slowed down, but elsewhere in the United States, Europe, the United Kingdom, Japan, Russia and Brazil, manufacturing output was accelerating.

An atypical crisis at the sectoral level: the crisis is a catalyst for the changes in capitalism. Without it, the developments of digital, e-commerce, telecommuting, and investments in the energy transition would not have been so rapid.

A salient example is the oil industry. Under pressure from investors and under the financial constraint of credit restrictions, the major oil companies are multiplying asset write-downs on oil fields and accelerating their investments in renewable energy. The fearful consequences of this crisis are likely to be capacity reductions in the supply of certain sectors such as textiles and certain parts of distribution, office real estate, restaurants, etc., and therefore, job conversions are expected.

An atypical crisis at the company level: crisis is usually synonymous with bankruptcies and increased defaults. But we have nothing of that sort to date. In the United States and Europe, default rates on high yield bonds are, according to the rating agency Moody's, only 7%. Admittedly, they ranged between 2% to 4% between 2012 and 2019 but, nothing like the 14% recorded in 2009 or the 12% in 2001. Similarly, in the OECD, i.e., in developed countries, non-performing loans are only at 2%, far from the 5% recorded in 2009 or 2001.

An atypical crisis at the monetary level: following monetary injections by central banks that were disproportionate to previous crises, long-term rates have hit historical lows, a level that is all the more unusual given that public debt has never been so high since 1945.

The recent rise in long-term rates is the result of three main factors: the sharp rise in oil and commodity prices that has raised fears of a temporary increase in inflation, the prospect of the use of an unprecedented savings stock, and the still very generous fiscal policies, such as the recent example of the U.S. stimulus package and an expected deficit of $3 trillion.

An atypical crisis at the financial level because savings rates have never been so high in the world. The savings rate, compared to 2019, increased by 11 points in Japan and the United Kingdom, by 9 points in the United States and by more than 5 points elsewhere. In France, for example, the savings rate has increased from 15% to 22% of gross disposable household income.

An atypical crisis in employment and wages: in Europe and Japan, the rise in the unemployment rate has so far been limited to less than 1.2 percentage points. This is thanks to partial unemployment compensation measures and bans on redundancies on economic grounds, for example in Italy, that will be in place until 30 June. As a result of the disappearance of low-paid jobs in the world, wages even increased in several countries in 2000.

An atypical crisis in terms of the decline in consumption: the fall in consumption has been unprecedented since the crisis of 1929 and in some cases, even greater. At the end of the third quarter, consumption in the United Kingdom was down 9 points from pre-crisis levels, 8 points in Spain, 7.8 points in the Eurozone and 6.5 points in Australia.

The composition of consumption is also unprecedented because consumers have not been able to afford services and have instead increased their purchases of durable goods.

At the slightest relaxation of containment rules, the rebounds observed in consumption are rapid and favoured by income resistance, and even increases in some countries like Australia, Japan, some European countries and the United States in 2020.

An atypical crisis for the stock market as price recovery has never been faster. There are several reasons for this – investors with excess liquidity that are not in the bond markets because of zero or negative rates, investors attracted by the performance of growth sectors and, investors confident in a rapid rebound in results.

In fact, growth stocks were the main investment theme in 2020 and led the recovery in prices and, unlike the technology bubble of the early 2000s, there were few disappointments in the results.

Cyclical stocks have taken over and, since the fourth quarter of 2020, have been the driving force behind the rise in the markets. Since the beginning of this year in the United States, in the oil sector – Exxon is up by 50% and Schlumberger by 32%, in the automotive sector – Ford is up by 52% and General Motors by 42%, in the airline sector – American Airlines is up by 48%, in the commodities sector – Freeport, a copper specialist, is up by 43% and, in the financial sector – Wells Fargo is up by 43%. If we take November as a reference month, the magnitude of the increases would have been greater and if we look at Europe, the trends are similar.

Today, some cyclical stocks still have the potential for appreciation, but defensive stocks will be added and certain growth stocks will be retained.

In conclusion, there are 9 surprising developments: a decline in bankruptcies despite the recession, an increase in savings despite the decrease in incomes, an initial fall in long-term rates to unprecedented levels despite an unprecedented increase in debt since 1945, a drop in unemployment in certain countries thanks to the subterfuge of partial unemployment, a record number of new businesses in several countries despite the cessation of activity in many sectors, strong appreciation of the stock market despite a fall in profits, strong appreciation of the commodity prices even though demand is far from returning to the pre-crisis level (for example, oil), a twelvefold increase in the value of Bitcoin ($5000 on March 12, 2020) but little change in the value of gold and finally, a substantial increase in the number of shareholders and IPOs of companies despite the crisis.

To conclude on an optimistic note, let us remember the OECD forecasts for global growth this year, recently revised upwards to 5.6% with expected growth of 12.6% in India, 7.8% in China, 6.5% in the United States, 5.9% in France, 5.7% in Spain and 3.9% in the Eurozone on average. In view of the third containment recently decided in many countries, these figures may be shifted by a quarter but the magnitude will be obvious.

Inflation, feared by some, will peak in the middle of the year but will then fall again as the base effects would have been absorbed.

The normalization of monetary policies is beginning in China and will continue in Southeast Asia but will not take place in the United States and Europe until 2023.

There are reasons to remain confident in the appreciation of the markets for some time and, like the king addressing ***Hamlet*** in the second scene of Act I of Shakespeare's play, we will say to the doubters, ***"Why are these shadows always on your forehead?"***

Geneva, 23rd March 2021

Bruno Desgardins

SINGALLIANCE
SingAlliance (Switzerland) SA-16bis rue de Lausanne 1201 Genève Switzerland
T: +41 22 518 85 85 │ www.sing-alliance.com

Bruno Desgardins
CIO
Switzerland

SingAlliance (Switzerland) SA
16bis rue de Lausanne
1201 Geneve
Switzerland
T: +41 22 518 85 85
E: info.switzerland@sing-alliance.com

SingAlliance Pte Ltd
20 McCallum Street
#18-01 Tokio Marine Centre
Singapore 069046
T: +65 6303 5050
E: info@sing-alliance.com

SingAlliance (Hong Kong) Ltd
1205, 12/F Bank of America Tower
12 Harcourt Road, Central
Hong Kong
T: +852 3611 7790
E: info.hongkong@sing-alliance.com