In for the long haul

The MAS eased policy in line with expectations this morning. Recent global market ebullience seems to be ebbing as stimulus measures are absorbed, but the virus data keep getting worse - this week we get the release of some potentially market-moving US data. This pattern of brief spells of optimism followed by lengthy spells of gloom is likely to persist

Source: Shutterstock

MAS eases policy

The Monetary Authority of Singapore (MAS) has grabbed centre stage on a quiet day for data releases today: Prakash Sakpal writes on this: "Consistent with their previous response to crises, MAS policy has moved to a neutral stance implied by zero appreciation of the S$-NEER policy band, albeit shifting the midpoint to the prevailing lower level. There is no change in the width of the band, estimated +/-2% from the mid-point. The statement reinforced a dismal growth and inflation outlook; growth projected between -4% to -1% and inflation between -1% to 0%. But, the central bank also emphasized “the primary role of fiscal policy in mitigating the economic impact of COVID-19”. However, a record stimulus of about 11% of GDP is only good once the Covid-19 threat to economy ends. Meanwhile, recession is unavoidable. A steeper than expected fall in 1Q GDP prompted a further cut to our 2020 growth forecast to -2.6% from -0.8%".

How will markets cope with months of train-wreck numbers?

Other central banks and governments have grabbed the headlines in recent weeks with their actions, just as the MAS has done today. But this pandemic is going to be a long haul. Have markets the stamina to remain buoyant over the coming months and the inevitable train-wreck of economic data coming down the tracks?

I think the answer is pretty obviously no. Last Thursday and Friday's market action seems to suggest that the positive impact of the $2tr US stimulus announcement has already begun to wear thin. To test this theory, this week, the US provides us with a wealth of potentially market-moving data, both sets of ISM numbers and the all-important non-farm payrolls figures on Friday. The consensus there is for a 100K decline in jobs. But the spread is wild, with the low at -1 million jobs, presumably encouraged by the recent initial claims figures. I'd like to see the market rally in the face of that.

Markets behaving more normally, but still some stress signs

We have begun to see some more normal bond/equity trading in recent days too, which is indicative of some of the Fed's financial plumbing actions beginning to work more normally. Bond yields are down to the mid-60s for the 10Y US Treasury now, declining along with equities. But the 3M Ted spread continues to widen, so there are still signs of financial stress evident. The Fed's work is not yet done.

Put that all together, and the medium-term trend for bond yields should be to resume its downward path, but that does not remove the possibility of occasional liquidity and loss-covering spikes, as we have seen at times in recent weeks.

Other Asian developments

(From Prakash Sakpal)

Malaysia: "The government's $58 billion (17% of GDP) stimulus package dwarfs those of most other countries given their sizes in terms of GDP. We expect Bank Negara Malaysia to waste no more time in announcing emergency rate cuts of the order of 50-100 basis points. However, as for most other economies in the region and the world, the stimulus should position the economy for a bounce-back once the pandemic ends, but in the meantime, it guarantees no lasting relief from the market sell-off.

India: Complementing the $22.6 billion (0.8% of GDP) fiscal stimulus package, the Reserve Bank of India on Friday announced emergency monetary easing via a 75 basis point reduction in the policy rate, 100 bp cut in the banks' reserve requirement, and $50 billion worth of liquidity support including targeted long-term repo operations and a three-month loan moratorium for banks and shadow banks. This may bring the economy back to its feet once the lockdown lifts in mid-April. Yet, the persistent gloom until and well after the end of Covid-19 is likely to be dragging the economy to its worst contraction ever and this is keeping markets and the INR under constant selling pressure".

And from Iris Pang on **China**, "It is reported that China is going to increase its fiscal deficit target in the coming Two Sessions. That is widely expected as the norm of that number is 3% to 3.5%, which is too low to offset the damage from Covid-19, and also was too low for 2019 due to costs to the economy from the trade war. From various official data, we estimate that the fiscal stimulus is 6.5% of nominal GDP for 2020, and it could increase to 8%-10% if there is a second wave of infection from imported cases".

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