
Global markets: What to watch for in May

Weekly Market Compass: Some countries and states are easing lockdowns, while politicians debate what to do next.

May 4, 2020 | Kristina Hooper, Chief Global Market Strategist

One month ago in this blog, I noted that April would be a critical month to gauge the global response to the COVID-19 pandemic. Across the board, it was a massive response, including significant monetary and fiscal stimulus from a variety of economies and widespread lockdowns designed to slow the rate of infection. But as we enter May, we are seeing differences in approach come to the fore – between countries, between localities, and between political parties.

How will we know which approaches are working to stem the rate of infections and to get people back to work? By examining the data. Here are some of the key issues that we will be watching in May:

Infection rates

Some European countries have begun to roll back lockdown measures, and some states within the US have also begun to loosen restrictions. The concern, of course, is that a second wave of infections may arise as a result, especially given that a number of the state rollbacks are occurring in contradiction of White House guidance that a loosening of restrictions should occur after 14 consecutive days of declining infection rates. And so we will be watching infection rates very closely for signs of a resurgence. If there isn't a second wave, that would certainly encourage other countries and other US states to open more areas of their economies. If, however, there is a second wave, restrictions may have to be reinstated, prolonging the period of time before economic activity can re-accelerate.

Earnings

We are in the midst of earnings season with 55% of companies in the S&P 500 Index having reported earnings, and 45% still left to report.¹ Importantly, much of the first quarter brought relatively normal activity before the pandemic spread in earnest. Therefore, from my perspective, the most important part of this earnings season is the forward guidance – and there has been relatively scant forward guidance on earnings from companies. FactSet Research found that, of the 122 companies that reported earnings as of April 24, only 50 (41%) discussed earnings guidance for 2020. Of those 50 companies, 30 said that they had withdrawn or were withdrawing previous earnings per share guidance for 2020 because of “the uncertainty of the future impacts of COVID-19.” Only 20 companies actually provided earnings guidance for the year: 10 lowered their previous guidance, six maintained their previous guidance, and four actually raised their earnings guidance. But while companies have not provided much guidance themselves, analysts have been slashing second-quarter earnings estimates at a dramatic clip. This is the single largest decline in a quarter's earnings estimates to be made by analysts in the first month of the quarter since FactSet began tracking this statistic in 2002. It would be helpful to hear from more companies about any forward guidance they can provide – or lack thereof – during this crisis even if it involves a variety of possible scenarios dependent on monetary, fiscal and health policy as well as medical outcomes.

The US Employment Situation Report for April

This is going to be an ugly report: According to Barron's, consensus estimates are for an unemployment rate of 16% and a loss of 21 million nonfarm payrolls. It could be even worse. Investors should expect the report to be shocking and not be caught by surprise - we have to keep in mind that there has been a dramatic drop in economic activity compressed into a very short time period, so the employment losses should be massive. What's more important than the job numbers is what policymakers are doing to maintain solvency in the face of this.

Negotiations about Phase 4 fiscal stimulus for the US

While the ink is barely dry on Phase 3.5 of fiscal stimulus passed just two weeks ago, I believe the US needs to see another fiscal package soon, particularly one that's geared towards state and local governments, as well as additional support for small businesses. This will not happen without serious debate, however, given Senate Majority Leader Mitch McConnell's suggestion that perhaps states should just file for bankruptcy - or at least they should not expect a check to "finance mistakes" not related to the pandemic. I believe a lack of economic support for states could be disastrous and only amplify the current downturn, given that state and local governments combined are a major employer. I suspect that we will see heated debate on this topic, but I believe that ultimately Congress will pass another stimulus bill that provides support for state and local governments, small businesses and other entities.

Possible re-ignition of the tariff war between the US and China

The United States is becoming more vocal in blaming China for the pandemic. Last Thursday, President Donald Trump threatened to apply new tariffs to China in retaliation. The next day, White House economic advisor Larry Kudlow also suggested there could be retaliation of some kind. We will want to follow this situation closely as any new tariffs would place more pressure on the US and global economies - and even the threat of such tariffs could significantly impact the stock market, as we saw in recent days. Over the last six weeks, the stock market has enjoyed a decoupling from the economy as a result of monetary and fiscal stimulus, but that could change with the risk of another tariff war.

Brexit negotiations

Yes, despite the pandemic, Brexit negotiations are continuing. If a deal is not struck by the end of 2020, the trading terms between the UK and European Union would default to World Trade Organization terms. This would be a negative development, especially for the UK, dealing a blow to an economy that has already been hit hard by the novel coronavirus contagion. We will want to follow this situation closely as well. Given COVID-19, there is certainly a very compelling rationale to extend negotiations beyond the end of 2020.

Data reports

There are several key economic data reports we will want to watch in the next month, including:

- US Retail Sales for April
- US Industrial Production for April
- China Retail Sales for April
- The University of Michigan Consumer Sentiment Index (preliminary)
- ZEW Financial Market Survey - economic sentiment for May

- UK Retail Sales for April
- IHS Markit Eurozone Composite PMI for May (preliminary)
- Eurozone Business Climate for May
- Eurozone Consumer Confidence for May
- US Consumer Confidence
- US Durable Goods for April

This economic data will give us a sense of where various economies are in terms of bottoming, in the case of most, and recovering, in the case of China.

Perhaps the biggest question I get from clients is about the shape of the economic recovery – whether we can rebound quickly into a V-shaped recovery, or whether we will linger at the bottom of economic activity for an extended period. As I have said many times before, I continue to believe that the shape of the economic recovery will be dictated by three policy prongs: health, fiscal and monetary. We’ve seen impressive steps in each category so far, but there is still a long way to go, and differences in approach are marking the path ahead. I expect May to shed more light on what’s working and what needs to be rethought, helping us get a better sense of the shape of that recovery.

Source

¹Source: FactSet Research Systems, as of May 1, 2020

Important information

The S&P 500® Index is an unmanaged index considered representative of the US stock market.

The University of Michigan Consumer Sentiment Index is published monthly, based on a telephone survey designed to assess US consumer expectations for the economy and their personal spending.

The ZEW Financial Market Survey is a monthly survey of about 350 analysts that measures economic sentiment in Germany for the next six months. The results are used to calculate the ZEW Indicator of Economic Sentiment.

The IHS Markit Eurozone Composite Output PMI is based on original survey data from IHS Markit’s Purchasing Managers’ Index surveys of both services and manufacturing. Purchasing Managers Indexes are based on monthly surveys of companies, and gauge business conditions within the manufacturing and services sectors. The opinions referenced above are those of the author as of **May 4, 2020**. These comments should not be construed as recommendations, but as an illustration of broader themes. Forward-looking statements are not guarantees of future results. They involve risks, uncertainties and assumptions; there can be no assurance that actual results will not differ materially from expectations.