

As COVID cases rise, will Powell address Fed tapering?



Kristina Hooper
Chief Global Market Strategist

Weekly Market Compass | August 23, 2021

Over the last several weeks, the idea that COVID-19 would soon be a problem of the past was dashed with recent data. Countries such as Israel — which I've described as the "gold standard" of vaccine rollouts — and the United States are experiencing a surge in COVID-19 infections. And, as I've referenced before, findings released by Israel last month indicated a growing decline in the infection protection of the Pfizer vaccine over time: While protection against infection for those who were vaccinated in April was at 75%, that figure fell to 16% for those who received their vaccination in January.¹ The good news is that the vaccine remained very effective in protecting against serious illness.¹

An Oxford study released last week, showed a similar — but not as severe — decline in efficacy over time, although that likely has to do with the shorter time frame of this study. The Pfizer vaccine was shown to be 92% effective in preventing infection in those with a high viral load two weeks after the second dose, but had declined to 78% by three months following the second dose.² AstraZeneca's effectiveness fell from 69% in those with a high viral load two weeks after the second dose, to 61% by three months following the second dose.²

And so we should not be surprised by the rise in COVID-19 cases in countries such as Israel and the United States, given that they were able to fully vaccinate earlier than other countries (especially Israel). It was reported last week that, for the first time since February, the United States reported more than 900,000 COVID-19 cases in the past week.³ This has driven home the aggressiveness of the Delta variant as well as the declining effectiveness of some vaccines. A look at statistics in one county of the United States — Los Angeles County — offers insight into this:

- In March 2021, breakthrough infections among fully-vaccinated county residents comprised just 2% of that month's total infections.⁴
- However, by June, when the Delta variant accounted for 50% of COVID infections in the county, breakthrough infections among fully-vaccinated residents accounted for 20% of all infections that month.⁴
- And by late July, when the Delta variant comprised more than 90% of all infections, breakthrough cases represented 30% of total infections.⁴

COVID data rattles US consumers

The resurgence of COVID-19 has cast a pall over consumer sentiment in the United States. The preliminary University of Michigan consumer sentiment reading for August clocked in at 70.2, a big tumble from the July final reading of 81.2.⁵ The gravity of this reading was underscored by the Michigan Surveys chief economist, "Over the past half century, the Sentiment Index has only recorded larger losses in six other surveys, all connected to sudden negative changes in the economy: the only larger declines in the Sentiment Index occurred

during the economy's shutdown in April 2020 (-19.4%) and at the depths of the Great Recession in October 2008 (-18.1%).”⁵

My takeaway from this reading is that headlines — especially around a scary, contagious disease that we still know so little about — can have a big impact on sentiment in a short period of time. This is illustrated by a recent poll by Morning Consult, which shows that 31% of Americans view COVID-19 as a severe health risk, up from 21% just a month ago.⁶

Mobility data remains solid

However, I am not going to let the consumer sentiment reading spook me. I think it is much more informative to look at mobility data. While more people say they are scared of COVID-19 and they feel worse about the economy, that hasn't stopped them from actually getting out and going to restaurants and shops— at least not yet.

Google's mobility data for the US (which looks at a simple average of retail and recreation, workplace, transit stations, and grocery and pharmacy stores) is showing only a slight slowdown as of Aug.19. It seems as though the only place most Americans still don't want to go is back to the office. Of course, we will want to follow mobility data closely to see if there is a negative impact from COVID-19 fallout in coming weeks.

Investor sentiment has fallen — but for how long?

Not only did recent COVID-19 data cast a pall over consumer sentiment, it cast a pall over investor sentiment as well. In the past week, the 10-year Treasury yield fell, major US stock indices fell, and oil prices were down while the VIX was up significantly. And the reality is that the COVID resurgence could cause a modest slowdown in some parts of the world, as it has in China (although that is the result of multiple factors, some unrelated to COVID). It could do so soon in the UK, the eurozone, Canada and other countries as vaccine effectiveness wears off. However, I continue to believe that it will just produce slight hiccups in the US and other countries that are willing and able to quickly roll out booster shots. In addition, the US Food and Drug Administration on Monday announced its full approval of the Pfizer vaccine, which could be a big help in encouraging more people to get vaccinated.

I should stress that it is not just COVID that is having an impact on markets; it is the narrative being adopted by many market participants that the Federal Reserve will begin tightening as economic growth is slowing due to COVID, hitting the US economy with a “double whammy.” Admittedly, that narrative was helped along by the release of the minutes for July's Federal Open Market Committee (FOMC) meeting, which showed that the Fed is moving swiftly toward tapering in the near future.

But we have to keep in mind that what happened at the July meeting was based on stale information — the COVID situation has changed a lot since then. Fortunately, Fed “hawk” and Dallas Fed President Robert Kaplan calmed market fears on Friday. He acknowledged that while so far the COVID resurgence has “not had a material effect on — based on high-frequency data — dining out, consumer activity,” it is having an impact in terms of delaying office return plans and the ability to hire workers given growing fears of infection.⁷ He recognized that COVID is the “big imponderable” and pledged he would closely follow the impact it has on the US economy. He suggested that, if it does have a material impact on the US economy,

he would advocate for an adjustment to tapering plans. This is significant because Kaplan was the first to call for the Fed to begin tapering.

All eyes on Powell's Jackson Hole speech

And so now Fed Chair Jay Powell's speech at Jackson Hole (scheduled for Aug. 27) takes on even more significance. There are some who expect his speech to be about cryptocurrencies, given references to crypto in the most recent FOMC minutes, and the Fed's development of a central bank digital currency, which is a related topic and one where there is ongoing research momentum at the Fed. However, I hold out hope that he will talk about tapering. More specifically, I expect him to reiterate that tapering is likely to happen soon and discuss details.

Of course, I would really like to see Powell amplify what Kaplan said last week — that the Fed will be willing to adjust tapering plans depending upon COVID's impact on the economy. I can't promise his speech will be as fun to watch as the newest episode of "Ted Lasso," but it's definitely going to be must-see TV at my house — popcorn and all.

Notes

¹The Times of Israel, "Israeli, UK data offer mixed signals on vaccine's potency against Delta strain," July 22, 2021

²Reuters, "British study shows COVID-19 vaccine efficacy wanes under Delta," Aug. 19, 2021

³University of Minnesota, Center for Infectious Disease Research and Policy, "US COVID-19 cases back to pre-vaccination levels," Aug. 16, 2021

⁴Deadline, "In Los Angeles, Breakthrough Infections Are Now 30% Of All New Covid Cases Amid Delta Surge," Aug. 19, 2021

⁵University of Michigan, "Surveys of Consumers, Preliminary Results for August 2021"

⁶Morning Consult, "The Return to Normal: Views on the Pandemic," Aug. 18, 2021

⁷Fox Business, "Fed's Kaplan watching COVID delta variant 'very carefully,' may 'adjust' views," Aug. 20, 2021

Important information

This does not constitute a recommendation of any investment strategy or product for a particular investor. Investors should consult a financial professional before making any investment decisions.

All investing involves risk, including the risk of loss.

The University of Michigan's 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 CBOE Volatility Index® (VIX®) is a key measure of market expectations of near-term volatility conveyed by S&P 500 stock index option prices. VIX is the ticker symbol for the Chicago Board Options Exchange (CBOE) Volatility Index, which shows the market's expectation of 30-day volatility.

Tapering is the gradual winding down of central bank activities that aimed to reverse poor economic conditions.

Cryptocurrencies are digital currencies that use cryptography for security and are not controlled by a central authority, such as a central bank.

The opinions referenced above are those of the author as of Aug. 23, 2021. 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.