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3 August, 2020

Things look rosy, but August and September are usually tricky

◆ Stocks maintain momentum as the second quarter earnings season nears its last chapter.

◆ So far, 83% of the S&P 500 companies that reported results beat expectations, helping to fuel the rally.

◆ The market focus could now shift to the virus and its vaccine progression as well as the availability and form of additional fiscal stimulus and the US presidential election.

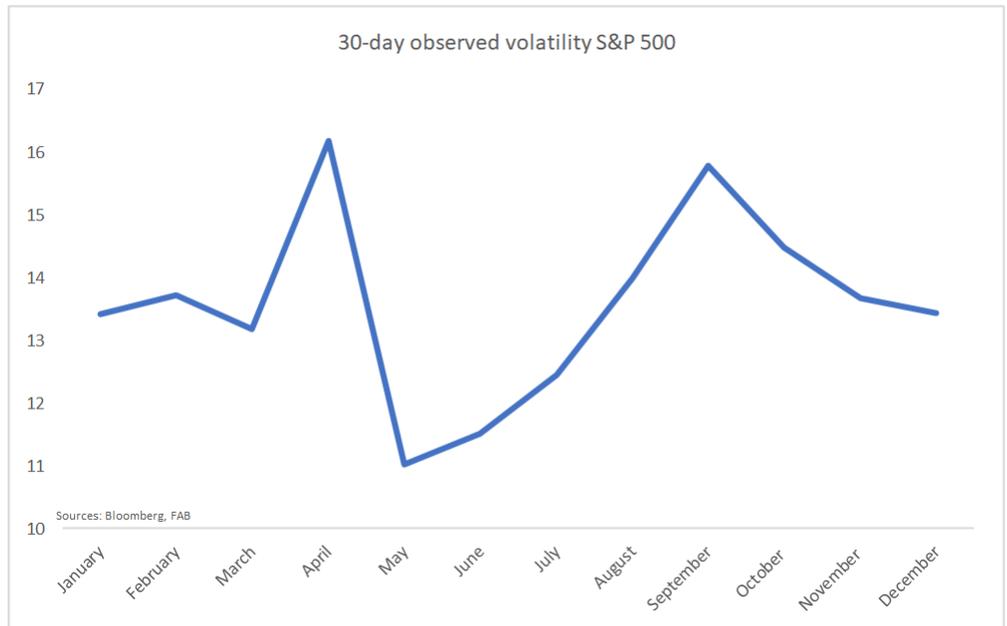
◆ To add to the concerns, August and September are traditionally more volatile than June and July.

◆ The FAB AAC remains overweight in investment grade corporate bonds and emerging market dollar debt.

Stock markets enter the month of August in a tear this year, even as the world economy continues to show signs of pain. The S&P 500 rose 5.51% in July while the Nasdaq Composite gained 6.82%. The broad index is now up 46.2% since its recent low on 23 March and the tech-heavy Nasdaq has gained 56.62%.

The gains in August were helped by better-than-expected earnings so far. Until Friday, 83% of the companies in the S&P 500 which had reported earnings had beaten analyst forecasts, much higher than the usual 70%-80%. This proved that analysts were overly bearish and prompted a leg higher for the market.

This push, however, is coming to an end. Unfortunately, looking ahead, there is plenty of uncertainty building up, much of which may not be fully priced into stocks and other risk assets.



Perhaps the most pressing concern right now is a spike in new coronavirus cases across the world. The State of Victoria in Australia, for instance, toughened its restrictions as cases there continue to rise. Manila, the capital of the Philippines, was heading to a lockdown again and in the UK the government of Prime Minister Boris Johnson was considering another lockdown in the City of London.

The prospect of closing these economies again weighed on risk assets with the Philippines Stock Exchange Index perhaps offering the best summary of the potential impact of such measures. The index dropped 3.58% today after President Rodrigo Duterte announced he was renewing the lockdown in Manila.

There is plenty of pushback from populations, and Germans took to the streets last week to protest the possibility of another lockdown. However, more restrictions cannot be ruled out.

Over the past 10 years, volatility has traditionally picked up in the third quarter

Investors may shrug some of the impact given their general expectation that monetary stimulus will continue to push risk asset prices higher. However, there is also some concern about the path ahead for fiscal stimulus. The US Congress is yet to agree on an extension for a number of economic support programs, just a week ahead of its summer recess. Failure to extend such stimuli could impact markets.

Then there is the US presidential election, which is less than three months away. If all that were not enough, August and September have been two of the most volatile months for stocks in the past decade. To be sure, any sell-off is likely to be met with more monetary stimulus. Still, things could be about to get interesting.

Investment Strategy Update

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