

For inquiries related to this article, please contact:

Alain.Marckus@bankfab.com

Christofer.Langner@bankfab.com

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Stocks rebound from sell-off as investors watch Powell

◆ **US stocks fail to breach key technical threshold as investors rethink valuations amid the current backdrop.**

◆ **Fed officials warn that further delays in reopening the economy could drag it into a deeper recession.**

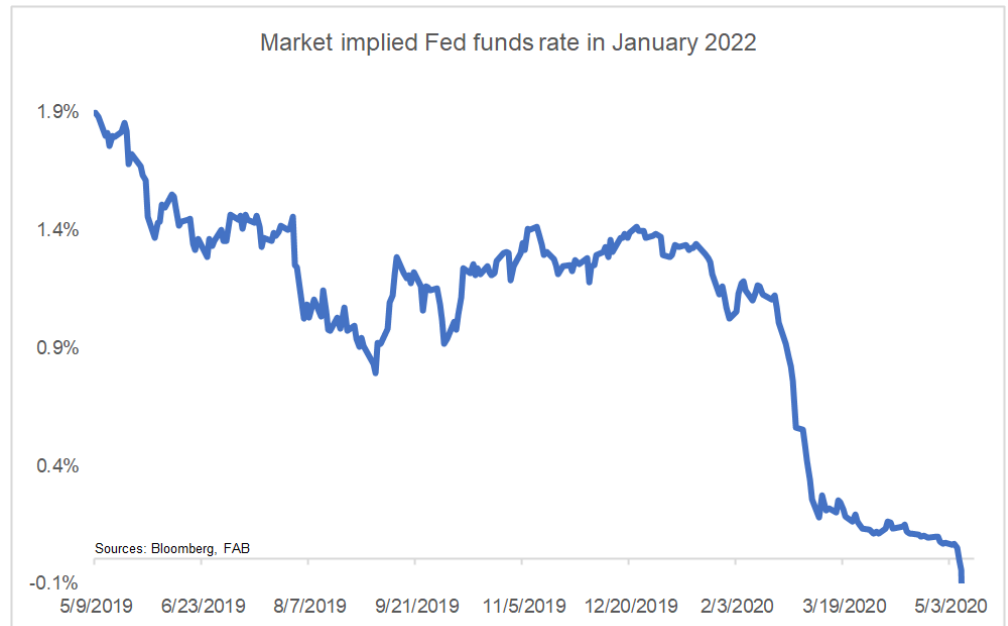
◆ **US top infectious disease expert Anthony Fauci tells Congress that Covid-19 could return strongly if reopening happens too fast.**

◆ **China closes off Jilin City as cases spike while Hong Kong sees its first new case in weeks.**

◆ **FAB AAC remains underweight in equities and overweight in gold.**

Stock markets sent a worrying message to the bulls yesterday after it retreated as the S&P 500 approached the key technical resistance level of 2,939. The S&P 500 fell 2.1% yesterday while the VIX volatility index jumped 5.5 points to 33, its biggest one-day rise since 20 April. Now, bears are closely watching whether the index drops below 2,727. News reports attributed the retreat to somber messages from Federal Reserve officials as well as warnings from the US's top authority on infectious diseases, Anthony Fauci.

The two messages conflicted. While Mr. Fauci said that the US risked a new outbreak of the new coronavirus if states and cities reopened too fast, St. Louis Fed President James Bullard said that keeping the economy closed for more than 90 days risks a round of bankruptcies that could create a depression-scale recession. For investors, either piece of news was bad. The prospect of more turmoil due to rising deaths was as terrifying as a depression.



The tone was a bit more positive today as investors looked forward to a statement by Fed Chairman Jerome Powell in hopes that he will offer a more optimistic view. The economic news was mildly good too, as the UK reported that its economy had shrunken 2% in the first quarter, better than the 2.6% retreat consensus forecast.

Even that, however, offered a grim picture. The UK's GDP shrank 6% in March alone, the latest report showed, despite the fact that the lockdown was only in effect for nine days of the month.

This has prompted the Bank of England to predict that the country's GDP will drop by a quarter in the first six months of the year, which would bring it back to the size it was a decade ago. A similar impact is likely in many other developed economies. Such a large drop may take years to reverse even if activity starts to normalize in the second half and raises the specter that a protracted recession may be possible.

The market is pricing in a high probability that the Fed will adopt negative rates by 2022

Investors have taken comfort in the fact that the fiscal and monetary response to this crisis has been significant and fast, two things that were lacking in the late 1930s, the last time the global economy faced a synchronized crisis of this magnitude. Then, governments were reluctant to spend and the newly created Fed did not see the value in adding liquidity. Scholars, many years later, attributed the length and depth of the depression to those policy mistakes.

This time, those policy mistakes are not being made. But Mr. Bullard's warnings suggest that there is a risk that governments are making other policy mistakes instead, such as keeping the economy in lockdown for too long.

Investment Strategy Update

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