Experts share latest developments on coronavirus, spiking oil prices and their impact on the markets

In this quickly changing world, we want to present you more updates from our subadvisors. We look at three critical areas: actions taken by the Federal Reserve, the energy sector, and the high yield bond market.

1. The measures announced by the Fed—and the fiscal measures under consideration—will help businesses stay open and will reduce the number of layoffs. The people who, thanks to the Fed or the government, keep their job, or have more cash in their pockets thanks to fiscal policy, will still not go to the mall, but they will shop online, they will order food for home delivery, they will not cancel their mobile phones. All this has a positive effect on spending today and through the contagion period.

2. Once contagion is contained and extreme social distancing stops, hopefully within 4-6 weeks, the economic recovery will be faster and stronger if more businesses have been able to stay open and more people have kept their jobs through the worst of the crisis.

3. This will be a temporary shock. Monetary and fiscal policy do not need to get people back to the shopping mall or on a flight, they need to keep them employed and spending on other things while the crisis lasts, and ready to go back to the mall or the airport when it stops. Monetary and fiscal policy are not expected to boost production in the factory facing weaker demand, they are aimed at helping the factory stay open until demand recovers.

4. Finally, putting in place extraordinary monetary and fiscal measures today is what will allow us to have a strong, hopefully V-shaped recovery once contagion is contained. As the health emergency recedes, having extremely supportive monetary and fiscal conditions already in place will make a massive difference.

The Fed Speaks Loudly And Carries A Big Stick
Sonal Desai, Ph.D., Chief Investment Officer
Franklin Templeton Fixed Income

The U.S. Federal Reserve (Fed) just announced (on Sunday, March 15th) a massive and well-crafted policy response to the coronavirus shock.

A number of commentators have quickly criticized it or dismissed it, arguing that no amount of monetary stimulus can get people back to the malls or the restaurants when they are worried about contagion. Some argue that for the same reason, fiscal policy will also be toothless. We could not disagree more, for the following reasons:

The Global Energy Sector
J. Gibson Cooper & René Ledis
Western Asset, a Legg Mason company

The global energy sector is facing a period of lower realized prices, uncertainty, and rising leverage.

This year is off to a tumultuous start to say the least, with volatility increasing in commodity markets. Leaving 2019 there was a semblance of stability creeping in that was welcomed by commodity markets. Oil demand growth was still present albeit at a slower pace, OPEC
High Yield Bond Market Update

Lord Abbett

High yield bonds, as measured by the ICE BofAML U.S. High Yield Constrained Index, posted negative returns over the year-to-date period as fears surrounding COVID-19 and oil price volatility led to a severe risk-off environment. Over the period, higher quality tiers of the high yield market outperformed lower quality tiers. The ‘CCC’ segment sharply underperformed the broader market, largely due to the selloff in the energy sector, overall investor sentiment and headwinds to price discovery in this lowest rung. High yield spreads started the year at 360 basis points (bps) OAS, and reached a low of 338 bps in mid-January. In late February, concerns surrounding the impact of COVID-19 on global growth intensified as the coronavirus spread globally.

In response to the coronavirus outbreak, the U.S. Federal Reserve (the “Fed”) cut the federal funds rate by half a percentage point on March 3rd. This move marked the first emergency cut by the Fed since December 2008. While stocks initially rallied in response to the surprise rate cut, any gains were erased soon after. Treasuries rallied as yields plummeted during the last week of February and early March as the market grew increasingly concerned of the implications surrounding COVID-19. The 10-year U.S. Treasury yield slid below 50bps heading into the week of March 9th, and the 30-year U.S. Treasury rate closed below 1%, which were 80-100bps below previous floors.

Markets received an additional catalyst for volatility in early March with the breakdown in the OPEC alliance and a price war between Saudi Arabia and Russia. Oil prices collapsed by more than 20%, stocks declined sharply and credit spreads widened over 100 basis points to an OAS of 668 bps in one session. As of March 12th, high yield spreads widened to 742 bps, which is nearly 400bps wider than year-end levels.
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Certain illnesses spread rapidly and have the potential to significantly and adversely affect the global economy. An outbreak of respiratory disease caused by a novel coronavirus designated as COVID-19 was first detected in China in December 2019 and subsequently spread internationally. The transmission of COVID-19 and efforts to contain its spread have resulted in international, national and local border closings and other significant travel restrictions and disruptions, significant disruptions to business operations, supply chains and customer activity, event cancellations and restrictions, service cancellations, reductions and other changes, significant challenges in healthcare service preparation and delivery, and quarantines, as well as general concern and uncertainty that has negatively affected the economic environment. These impacts also have caused significant volatility and declines in global financial markets, which have caused losses for investors. The impact of this COVID-19 pandemic is expected to be short term or may last for an extended period of time, and in either case could result in a substantial economic downturn or recession. No guarantee or representation is made that investment objectives and/or opinions stated will be achieved. Each specific client’s or investor’s experience may vary.

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GE-3010227 (3/20) (Exp. 6/20)