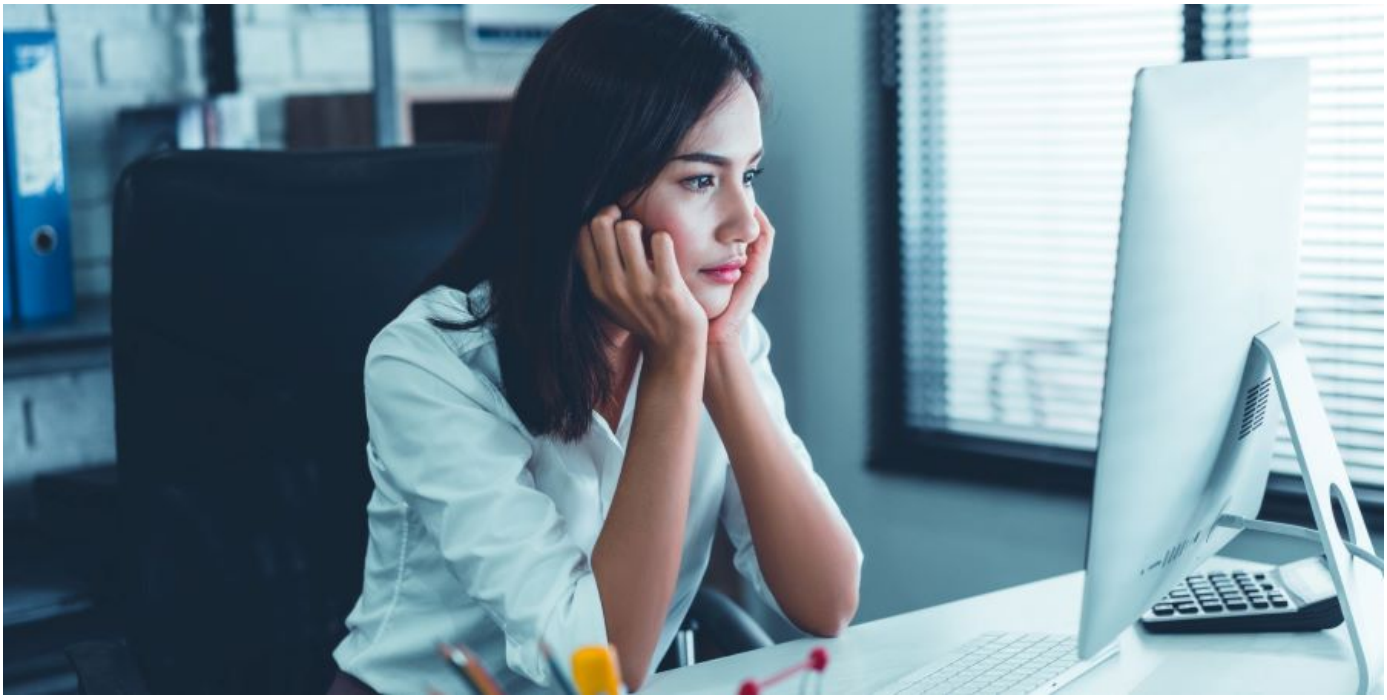
Invesco Canada blog

Insights, commentary and investing expertise

Kristina Hooper | October 1, 2020



Five questions we're hearing from investors

There is a feeling of apprehension in markets. I can sense it in the questions I receive. I continue to get more run-of-the-mill queries such as: "Are stocks still overvalued at current levels?" But then there are the new questions, which reflect deeper concerns. Most of the election-related questions I have received are like none I have gotten before in my career.

What if there is a second wave of COVID-19?

Infections have spiked in a number of European and North American countries. I am hopeful that there won't be a major second wave, but I believe there is a good possibility that there will be one. However, enough has been learned about managing the virus that even if there is a major second wave, I expect hospitalizations and especially deaths to be lower. If there aren't a high level of hospitalizations, then I would not expect to see the massive lockdowns that we saw with the first wave. (Of course, that may not necessarily be the case. Israel just entered a second lockdown in response to a second wave of COVID-19 cases.) But if it is the case that most countries are able to avoid wide-scale lockdowns, the negative impact to the global economy should be relatively low, in my view, although we should expect a drop in mobility as some individuals choose to self-quarantine. While a rise in infections would spook the stock market, I would expect that reaction to be very temporary if it doesn't result in major lockdowns.

Will it matter for the US economy if there is not another fiscal stimulus package?

Yes, it is a concern for the US economy. Federal Reserve Chair Jay Powell has stressed that, while the economic recovery has been faster than expected, the path ahead remains highly uncertain – and a lack of fiscal stimulus would hurt the economy. Just last week in testimony before the Senate Banking Committee, he reminded that there are still 11 million Americans without jobs and therefore there is a lot of work still needed to help them.[1]

What we are seeing from the mobility data is that economic activity has already flatlined in the US, which suggests that economic growth is slowing (and that could only worsen if infections rise). This is borne out in some recent data. For example, US durable goods orders rose for a fourth straight month in August, but they rose at a far more modest level.[2] Until there is a vaccine, I believe it will be difficult to achieve any major increase in economic growth. Fiscal stimulus is the lifeline that keeps the economy going while it is waiting for the end of the pandemic, and there are a number of areas that need support, in my view, such as state and local governments.

I still think there is a chance we could get another fiscal stimulus package in the US (after all, the White House recently signaled it might be open to a more robust stimulus package than proposed by Senate Republicans). However, the stock market seems to have accepted the notion that there will likely not be another fiscal stimulus package before the election. Therefore, if the economic data remains stable, I don't think stocks would react negatively to a lack of additional stimulus.

What do the Fed's actions mean for stocks?

It should become increasingly clear to markets that the Fed's change in inflation targeting policy is a very important development. Simply put, the Fed has gotten more accommodative, and its projections of interest rates remaining near zero through 2023 should drive home the notion that rates will be lower for longer. I know the stock market was disappointed that the Fed didn't increase quantitative easing (QE) purchases at its last meeting, but it can always do that later, when it feels that approach is needed. In fact, the Fed has made it easier to increase QE going forward by expanding the rationale for it. Previously it said it would increase QE to sustain "smooth market functioning," but in the September Federal Open Market Committee meeting it decided it would also increase QE to "help foster accommodative financial conditions." This will give the Fed greater flexibility to increase QE purchases going forward. Even without increased QE, the monetary policy environment is very supportive of risk assets such as stocks.

What happens if there is a contested presidential election?

As we imagine the possibilities for what might occur in November's US presidential election, I believe we can look to election night 2016 as a guide to what can happen in a contested election. As you may recall, US stocks dropped dramatically overnight and gold rose modestly, only to recover the next morning. At the time, the narrative around these moves was that the stock market feared a Trump presidency. However, I suspect the more likely explanation is that the drop occurred because Hillary Clinton did not concede the race until the next morning, and the stock market was fearing a contested election.

I imagine this reaction could happen again, as markets are already fretting over a contested election. I would expect stock market volatility and short-term stock market sell-offs in the weeks leading up to the election. In this environment, I would expect gold and Treasuries to perform well. If in fact we do have a contested election, that investing environment could continue until there is a resolution. I believe investors need to be prepared for that possibility – but how? That brings us to our final question.

What does all of this mean?

I firmly believe that it's important to focus on long-term goals and to try to ignore the short-term noise and volatility – and to remain well-diversified both across and within major asset classes such as stocks, bonds and alternatives. One of the biggest lessons that many investors learned during the Global Financial Crisis is that abandoning stocks due to fear may cause you to lock in losses and miss out on meeting your financial goals. With stocks having sold off significantly already, I believe this might represent an attractive opportunity – especially in the tech sector, which, as I explained in a previous blog (https://blog.invesco.ca/three-reasons-isnt-another-tech-bubble/), I expect to benefit from the Fed and pandemic-related themes.

It may be reassuring to know that the tension between short-term noise and long-term fundamentals is nothing new. The economist Benjamin Graham (1894-1976) once said that stocks are like a "voting machine" in the short run but a "weighing machine" in the long run. In other words, over the longer term, stock prices reflect the measure of a company's fundamentals, but over the shorter term they can reflect investors' fluctuating emotional reactions to news flow, economic data, and even rumors. In election years, the "voting machine" atmosphere can be amplified given the daily (or even hourly) headlines about candidates' policy announcements and polling results. And so investors today need to be even more vigilant about ignoring the noise and looking ahead to their goals, no matter how difficult that becomes.

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1 Source: MarketScreener, "Mnuchin Says Fed Lending Programs Have Done All They Can," Sept. 22, 2020

2 Source: The Wall Street Journal, "U.S. Durable-Goods Orders Rise for Fourth Straight Month," Sept. 25, 2020

Important information

Blog header image: Credit: Torwai / Getty

Diversification does not guarantee a profit or eliminate the risk of loss.

All investing involves risk, including the risk of loss.

Quantitative easing (QE) is a monetary policy used by central banks to stimulate the economy when standard monetary policy has become ineffective.

The opinions referenced above are those of Kristina Hooper as of Sept. 28, 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.