THE ECONOMIC MONTH IN REVIEW AND OUTLOOK – NOVEMBER 2020

U.S. Markets and Economy

U.S. stocks had an explosive November. The Dow Jones Industrial Average rose 4,000 points to break the psychological 30,000 barrier. The broad-based S&P 500 index rose more than 10% for the month (which is normally considered a good showing for an entire year), and the Nasdaq Composite rose more than 1,000 points to break decisively above the 12,000 level. What was the market celebrating? Three things: a settled election, excellent vaccine progress, and a "pedal-to-the-metal" Fed.

First, the initial uncertainty about the outcome of the presidential election was essentially eliminated, as the electoral votes in several key swing states were awarded officially to former Vice President Joe Biden after recounts and court challenges. The Democrats won the presidential prize but lost seats in the House and are unlikely to gain control of the Senate after the Georgia runoffs in early January. Wall Street generally likes divided government, so this was close to an ideal outcome for traders. Biden's early cabinet picks include Janet Yellen as Treasury secretary, which cheered markets both because it wasn't Elizabeth Warren and because Yellen has the extensive experience and first-rate technical skills to manage fiscal policy in the COVID-19 era (she is respected by all parties).

Second, the U.S. may have several effective vaccines to choose from in the coming months, with two (those from Pfizer and Moderna) showing 95% effectiveness in their initial tests. AstraZeneca may have also crossed the initial finish line with their vaccine, but virologists are troubled by the design of their study. Other vaccines may also demonstrate efficacy in the next few months. The next step will be mass immunizations in the U.S. (and the rest of the world), which could bring the virus under control by the second half of 2021. Although the full-scale manufacturing, distribution, and administration of all these vaccines will pose problems, they are likely to be resolved during the year to come.

Third, the Fed, whose expansionary monetary policy has played a key role in keeping the COVID-19 recession from turning into another Great Depression, has stated that it plans to keep both feet on the monetary accelerator far into the future. Short-term interest rates will remain at zero, and with continued purchases of long-term Treasuries, corporates, and muni bonds, long-term rates will stay very low. The U.S. 10-year yield remains below 1%, which is actually negative in real terms, as inflation is running at a little more than 1%. Low rates encourage borrowing for automobiles and other consumer durables and also make mortgages, for both home purchases and refinancing, very attractive. The U.S. housing market is thus quite strong, which further drives the economy forward.

World Markets and Economy

In London, the FTSE 100 blue-chip index had an even more powerful rally than Wall Street in November. This rally is something of a mystery, because the British are heading toward a last-minute collapse in Brexit negotiations that will certainly drag down the British economy. In late November, the French tested post-Brexit no-deal immigration rules, and it created a massive traffic jam of trucks on the British side. A vaccine will be powerless to stop the economic chaos.

The rest of Europe also surged, with double-digit gains in most stock indexes. The Paris Bourse gained almost 20%. The main story is that with vaccines coming, European economies can emerge next year from punishing lockdowns even while the virus surges now, including in countries that had it under control in the summer.

Japanese stocks had a tremendous November too, also rising at a double-digit rate. Even better, the Nikkei index is now higher than it has been since the 1990s. Asian counties have also signed a new trade deal that will expand markets for Japanese exports. At the same time, new Prime Minister Suga has also pushed for more stimulus spending to keep economic growth positive.

The Shanghai Composite also rallied, bringing it to its highest level of the year. The Chinese economy will be the only major economy to grow in 2020. Nonetheless, China faces growing hostility from the U.S. Many Chinese stocks may be delisted from U.S. exchanges, and more companies may be banned from doing business with the U.S. government. Biden is unlikely to soften his approach to China and may keep, as bargaining chips, all the tariffs imposed by Trump. The Chinese international aggressiveness toward Hong Kong, Taiwan, India, and even Australia may raise international tensions, which could slow growth everywhere.

Outlook

In the short run, global economic growth could again come to a halt as the U.S. and many other countries begin locking down their economies to control a powerful new wave of viral infections. These lockdowns could persist until vaccines finally crush the virus. At that point, world economies could see very strong economic rebounds that stock prices, especially in the U.S., are clearly predicting. Although the economy will not instantly recover to its pre-COVID level, an increase in personal consumption (70% of GDP), as vaccinated Americans begin to return to their old spending habits, could fuel strong growth, especially in the second half of the year.

With the incoming Biden administration potentially finding a way to compromise with Congress to fund infrastructure investment (the U.S.'s needs are in the trillions of dollars), more spending on science and research, and new spending to move toward a greener economy, fiscal policy should also on net be a driver of economic growth in the short and long run. Unfortunately, the pandemic outlook for the next few months is poor, with the numbers of cases, deaths, and hospitalizations soaring as Americans spend more time indoors (which epidemiologists argue accelerates the spread of the virus). The arrival of effective vaccines provides a light at the end of the pandemic tunnel, but, for this winter, the world is still in the dark part of the tunnel.