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Economic Outlook

Third Quarter 2020

Regime Change

By: James R. Solloway, CFA, Chief Market Strategist and Senior Portfolio Manager

SEI recently released its third-quarter Economic Outlook. A summary of the conclusions is provided below:

- COVID-19 remains a significant public health concern that continues to hamper the global economy, and there is no disputing that US economic activity remains far below normal.
- Incomes are now recovering as more people get back to work. Still, the danger exists that the lack of additional income support will drag down consumer spending heading into year end. It's concerning that consumer and business sentiment remained depressed.
- SEI doubts that there will be a full return to normal economic behaviour until the introduction and global distribution of vaccines that are safe and effective. Positive news of vaccine development (along with the massive fiscal and monetary response) contributed to the buoyancy of equities and other risk assets during the quarter.
- The US presidential election will have a major impact on the economy and financial markets in the months and years ahead. Yet, we firmly believe that it is a mistake to base even a short-term investment strategy that requires picking November's winner; predicting the policies proposed by the new president; figuring out how those proposals will be modified by Congress on their way to becoming actual laws; and forecasting the impact those new laws would have on the economy and financial markets.
- According to the Federal Open Market Committee's official projections, the federal-funds rate is expected to stay near 0% through 2023[1]. Fed Chairman Jerome Powell recently unveiled a framework for the conduct of monetary policy. Rather than taking pre-emptive actions against inflation when US unemployment reaches a level that might cause inflation to rise, the central bank will now wait for an actual worsening of inflation pressures before responding.
- UK Prime Minister Boris Johnson is facing a rebellion among his own backbenchers and intense criticism from senior Conservatives over his proposal to renege on the withdrawal treaty that would allow Northern Ireland to trade without border restrictions with Ireland and the rest of the European Union. The move to abrogate the treaty would almost certainly lead to a hard Brexit.
- Obviously, a hard Brexit will not help matters. But the worst impact potentially will be sustained by financial companies and other service-producing entities, since World Trade Organization rules deal mostly with tradable goods. The increase in tariffs, for the most part, will be bearable—once border-related issues are worked out.
- In our view, it is unlikely that radical changes will be made to the direction of policy under new Japanese Prime Minister Yoshihide Suga. The near-term priority will be on the response to the coronavirus, and fiscal policy will remain quite expansionary. The Bank of Japan will continue to buy most of the bonds that the government issues, along with other types of corporate debt and equity.
- There is some good news, which applies to emerging markets more broadly. The price of raw industrials bottomed in early May and have since enjoyed a sharp move higher. If industrial commodity prices advance in a sustained, multi-year fashion as they have in previous cycles, it's a good bet that emerging-market corporate profits will rise sharply.
- In uncertain environments, we believe it is important to maintain a risk-aware approach to wealth management through prudent planning that focuses on companies with strong fundamentals and reasonable valuations.

A full-length paper is available if you wish to learn more about these timely topics.

[1] Source: US Federal Reserve. Data as at 30/9/2020.

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