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Erik Britton



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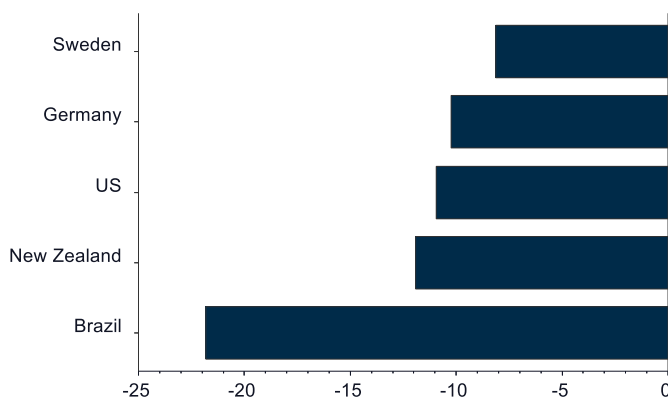
Headlines

- President Trump contracts COVID, encourages others not to let the disease dominate their lives
- V-shaped recovery remains our central case, but W is a growing risk
- Second wave of infections happening in earnest in Europe, but fatality rates still low, for now
- Jury still out on how to balance the health and economic impacts of the virus, and on the best policies to control it
- Still a risk-off year in financial markets to date, with a handful of risk assets bucking the trend, and looking topky as a result
- Trade flows collapsed across the G4 in the first half of 2020, slight bounce-back into Q3

Managing the impact of COVID-19 on social welfare requires careful consideration of both economic and health outcomes. The ideal strategy to maximise social welfare would minimise the trade-off between those two concerns: simultaneously reducing to a minimum both the health costs and the economic costs of the virus, now and in expectation. But the experience across countries so far suggests that this ideal strategy is difficult to achieve in practice. At one end of the spectrum of policy responses is New Zealand, where deaths from the disease per million inhabitants have remained extremely low throughout, while the economic costs are around the middle of the pack, suggesting that policymakers there prioritise health outcomes over economic outcomes. At the other end is Sweden, where the economic impact has been relatively small, while the number of deaths per million inhabitants is relatively large, suggesting a more equal weighting between health and economic outcomes than in New Zealand. Other countries, such as the UK, have seen very large impacts on both the economy and health, suggesting that any policy objective in the UK has been relatively poorly executed compared to other countries - at least, so far. That conclusion is, sadly, reinforced by the UK government's absurd and costly recent error in data management, springing from an ill-judged choice of data storage software, which would have embarrassed a schoolchild.

GDP change 2019 Q4 to 2020 Q2

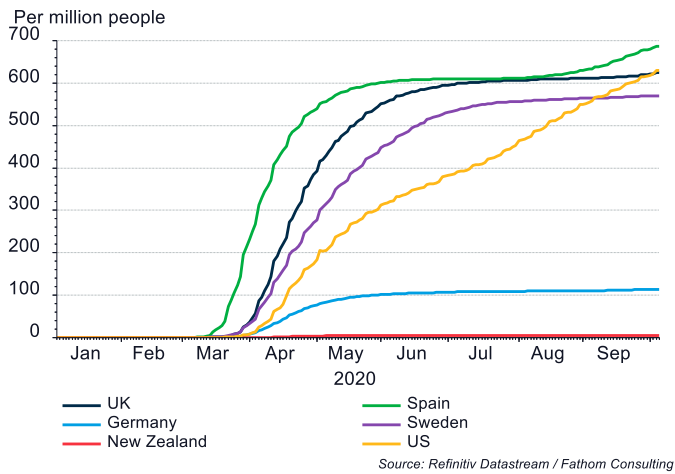
Percentage changes



Source: Refinitiv Datastream / Fathom Consulting



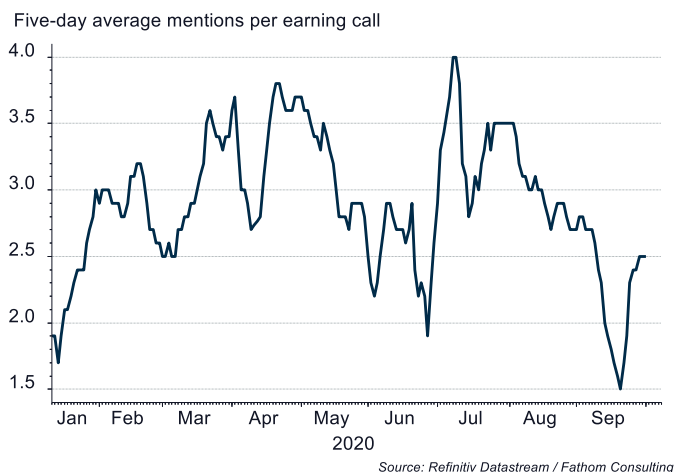
COVID-19 deaths



It is not clear, yet, which strategy is the 'best' (although there is increasing clarity about which are the worst). The number of new cases is undoubtedly picking up across many countries now, especially in Europe, though so far the fatality rate in the second wave remains encouragingly low. Even in Spain, where the fatality rate is accelerating, the path of the second wave is not - yet - close to what we saw in the first wave. In the UK, the line is starting to pick up again, but so far it barely registers compared to the first wave. In Sweden, there is no discernible increase at all, so far, in the number of deaths per million, while New Zealand remains exceptionally low. There has in the past been a lag of several weeks before increased infections started to show in data on rising fatalities, and it is likely that the fatality rate will increase in most countries. But, in our central case, it will not repeat the rate of increase we saw in the first wave, for reasons elaborated in previous *Fathom Recovery Watches* and elsewhere.

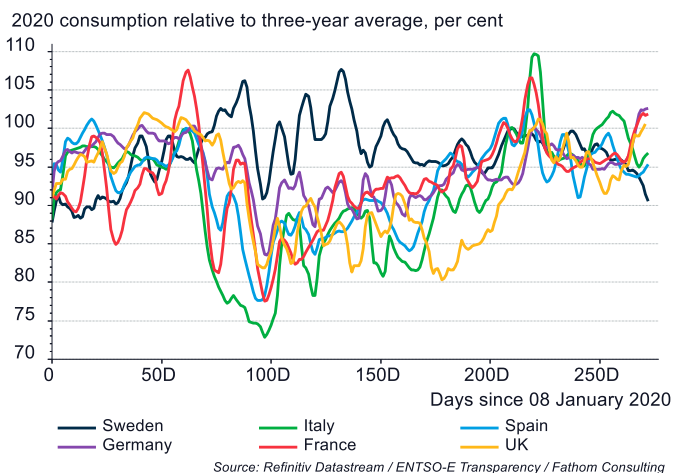
Early in September, we were strongly persuaded that our central, V-shaped recovery scenario was correct - supported by very low pressure on corporate earnings at that time according to our proprietary measure, and by the fact that electricity consumption had come back almost to normal levels for the time of year across many European economies. Since then, however, the news about rapidly rising new cases has sown a seed of doubt. A 'V' remains our central case, but the risk of a 'W' is increasing - particularly in Sweden.

Margin pressure gauge in corporate earnings call



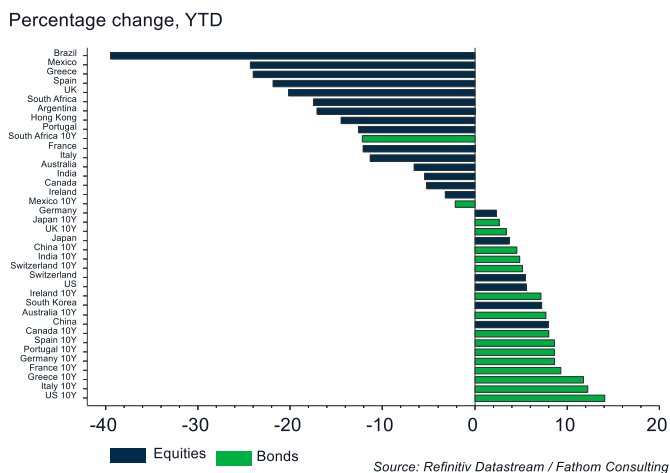


Electricity consumption



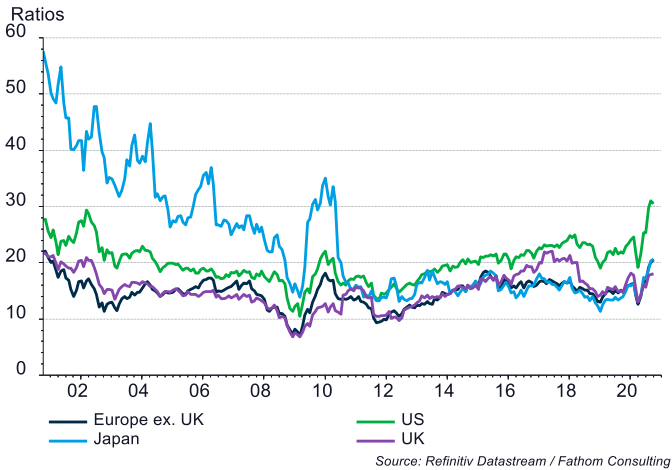
The general economic impact of the crisis is severely negative through 2020 so far. In financial markets, that translates into risk assets selling off while safe assets prosper. As the chart shows, that is on the whole what we have seen through 2020 to date: equity returns (expressed in dollars) have fallen in most countries, while bond returns have rallied. There is a handful of exceptions, including the US equity market, where equity returns are up in high single digits so far this year. That strong performance reflects massive stimulus from macroeconomic policy that has resulted in a strong if, as yet, partial rebound in economic activity from the April lows. And it also reflects the fact that the US economy in the round is regarded as a safe haven, so even risk assets like equities tend to outperform equities in other countries when the mood is risk-off globally. But the result is that US equity prices now look topy, with the PE ratio rising to levels not seen since the dotcom boom of the early 2000s.

Equities and bonds total return index, USD



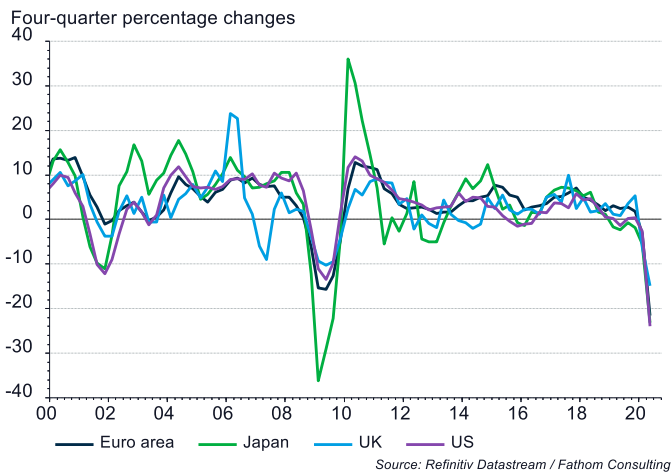


PE ratios



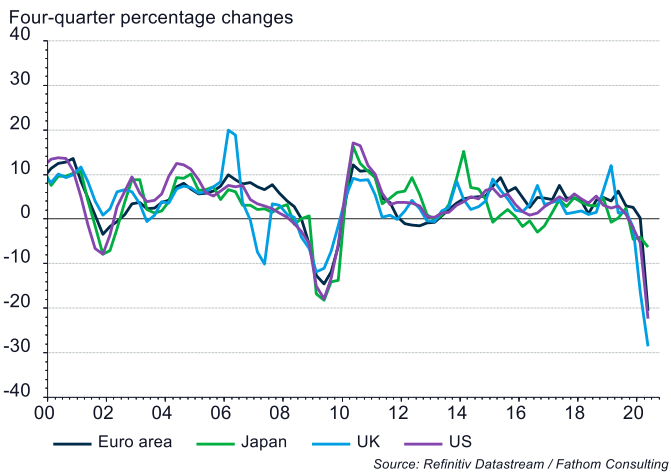
Trade flows collapsed in the first half of 2020, with both imports and exports of goods and services down in big double digits across most advanced economies compared to a year earlier. The fall in trade eclipses even the experience of the Great Financial Crisis (GFC) of 2008/09, and represents a further step down in trade as a share of global GDP - a metric that had been increasing since the industrial revolution. That increasing trend was partially reversed during the GFC and trade has fallen again in 2020, having flatlined in between. If trade stays lower permanently, it will prove costly for the growth of the global economy in the long run: item 1 in international macro 101 states that trade is good for growth, and more trade is better.

G4 exports



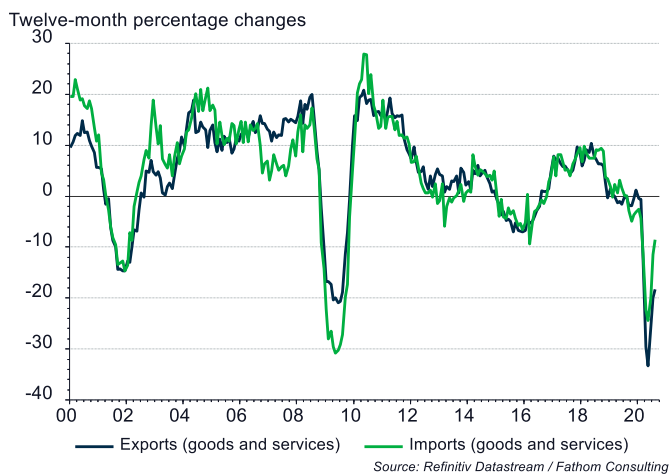


G4 imports



The signals into Q3 so far are not encouraging: US trade flows in both directions are still down substantially on a year earlier (to August, the latest data available). The growth rate will eventually turn positive, but it is likely that the pre-crisis trajectory for trade as a share of GDP will never fully be restored.

US exports and imports





Interesting reading

- Was the virus manmade? Some say yes: <https://www.express.co.uk/news/world/1344201/China-coverup-news-coronavirus-dr-yan-li-meng-yan-whistleblower-Beijing-steve-bannon-miles>
- Others cite clear evidence that the virus evolved naturally: <https://www.nationalgeographic.com/science/2020/09/coronavirus-origins-misinformation-yan-report-fact-check-cvd/>
- Bond market volatility calmed by Fed balance sheet: <https://themarketear.com/posts/cbjwz0ksCu>
- The WSJ reports that offices in Manhattan remain much emptier than those elsewhere in the US: <https://www.wsj.com/articles/manhattan-offices-are-nearly-empty-threatening-new-york-citys-recovery-11601371800>
- Heterogeneity in propensity to spread the virus is a key factor in its propagation: <https://www.theatlantic.com/health/archive/2020/09/k-overlooked-variable-driving-pandemic/616548/>
- A better way to express the risk of COVID-19: <https://www.bmj.com/content/370/bmj.m3259>



Fathom Consulting
47 Beviden Street
London
N1 6BH
Tel: +44 (0)20 7796 9561



Contact information
erik.britton@fathom-consulting.com
0203 879 9811
www.fathom-consulting.com

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