Despite the doubts, the financial markets continue to recover

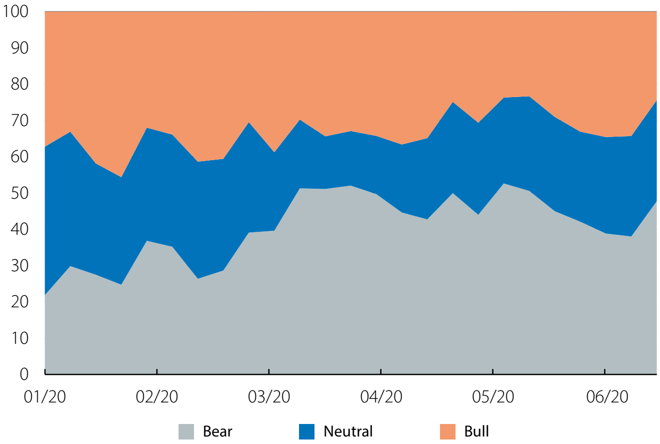
Investors debate between recovery and resurgence. We have now left behind the weeks of March when the paralysis of most economies due to the COVID-19 outbreak and a large dose of uncertainty among investors led to the biggest collapse in the financial markets in several decades. Since then, the powerful monetary and fiscal stimuli from the central banks and governments, as well as the gradual lifting of social distancing measures, have fuelled investor sentiment and facilitated an appreciation of riskier assets, such as equities, speculative-grade corporate debt and commodities. However, following this stabilisation of sentiment, investors have acted more cautiously in recent weeks. In June, the markets also maintained a positive tone but risk appetite was more restrained, as the economic data have confirmed that the decline in economic activity in recent months has been very sharp and the projections continue to suggest that the economic recovery will be gradual and dependent on the absence of new outbreaks (indeed, in June there were sessions marked by financial volatility due to a rise in cases, especially in the US and Latin America).

The stock markets register gains in an uncertain scenario. Since the heavy losses endured in the stock markets in March, equities have registered significant gains around the world (the global MSCI index is up 35%), despite still being down on a year to date basis. The recovery of the stock market indices has occurred unevenly between regions, mainly due to the sectoral composition of each index and their differing price multiples. Nevertheless, some of the common aspects that have supported gains across the board include the improved economic outlook and the wide range of fiscal and monetary stimuli. The most representative example lies in the US and European stock markets, where the decisive responses from the Fed and the ECB and the EU's proposed Recovery Fund boosted investors' risk appetite in June (EuroStoxx 50 +6.0%, S&P 500 +1.8% and Nasdaq +6.0%). However, this buoyancy in stock prices was not free of volatility. There were several sessions in which the rise in COVID-19 infections and institutions' caution regarding the pace of economic recovery dragged the stock indices down.

The oil price moves clear of its recent lows. Another asset that followed a very similar path is oil. In June, the price of a barrel of Brent continued to rise, reaching over 43 dollars, a level not seen since the beginning of March. This rise was due to a gradual acceleration in the demand for fuel (linked to the restoration of activity in most countries and the improvement in investor sentiment) and the continuing decline in supply from OPEC and its allies. Indeed, this latter factor gained prominence following the extension of the agreement to cut production by 9.7 million barrels a day until the end of July (initially, the cuts were due to be relaxed starting in early July)

US: market sentiment

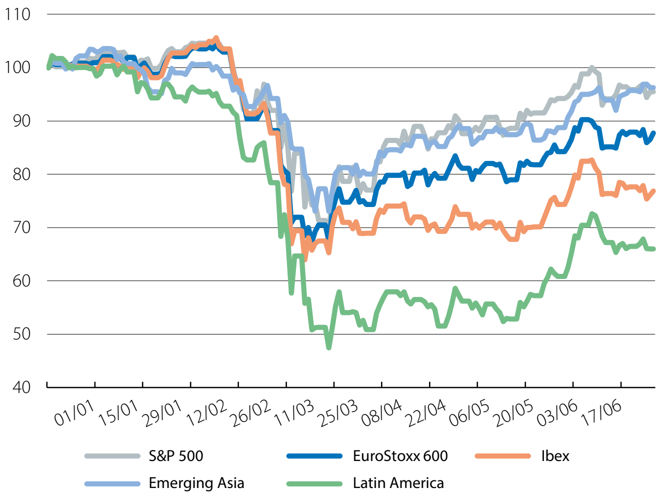
(%)



Note: *Percentage of investors who respond to the American Association of Individual Investors sentiment survey: bull, bear or neutral.*
Source: *CaixaBank Research, based on data from Bloomberg.*

Main international stock markets

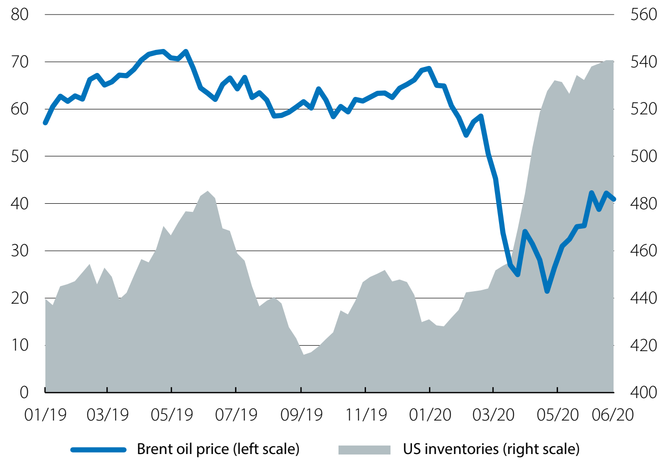
Index (100 = January 2020)



Source: *CaixaBank Research, based on data from Bloomberg.*

Oil: price of a barrel of Brent and US crude oil inventories

(Dollars per barrel) *(Million barrels)*



Source: *CaixaBank Research, based on data from Bloomberg.*

and a stricter enforcement of the production quotas among its members. Meanwhile, the price of a barrel of WTI (West Texas Intermediate, the benchmark oil price in the US, which in previous months had temporarily fallen to negative prices) was also boosted by activity being halted at several shale extraction wells and rose to 38 dollars.

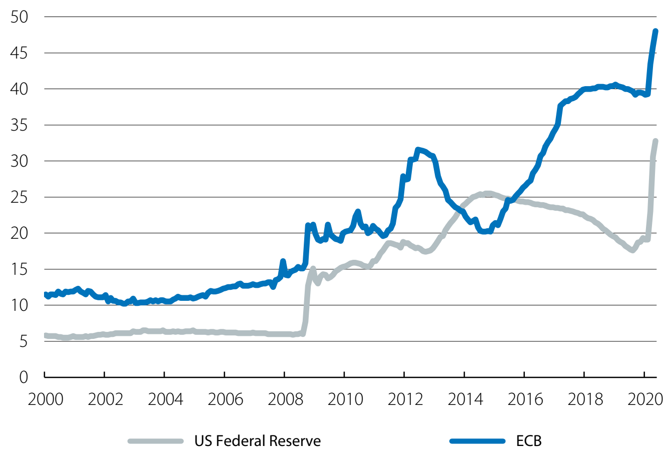
The ECB redoubles its efforts to combat COVID-19. At its last meeting in June, the bank presented a gloomier view of the economic outlook (it estimates that euro area GDP will fall by around 9% in 2020, although it also offered a more severe scenario in which it could fall by 12.6%), despite the signs of incipient recovery from some economic activity indicators. For this reason, and in an attempt to ease the financial and economic tensions that could arise from such an uncertain scenario, the ECB announced significant measures: (i) a 600-billion-euro increase in the pandemic emergency purchase programme (PEPP), which will be added to the 750 billion already announced in March, (ii) the extension of the PEPP until at least June 2021 and (iii) the reinvestment of the principal of PEPP maturities up until the end of 2022. These measures were in addition to other existing asset purchase programmes and official interest rates being kept at their historical lows. In addition, liquidity injections reached a historic peak in June, with demand for June's TLTRO reaching 1.3 trillion euros (a net increase in liquidity of 548 billion euros, after discounting the portion corresponding to refinancing previous operations).

The other major central banks are also expanding dovish measures. Like the ECB, other central banks took further steps to address the adverse economic scenario triggered by the pandemic. On the one hand, the Fed facilitated access to some of the programmes aimed at supporting corporate credit and hinted at the possibility of controlling the sovereign yield curve through its participation in the treasuries market, like the Bank of Japan is already doing. On the other hand, the Bank of England increased the total sovereign debt it intends to purchase by the end of the year by 100 billion pounds (to 745 billion). Similarly, in emerging economies, China's central bank cut the repo rate to 2.35%, while in Brazil official rates fell to new historic lows (2.25%).

Yields in the euro area periphery continue to decline. In June, the ECB's actions through the PEPP and the fourth TLTRO auction continued to favour a decline in long-term yields in the debt of the euro area periphery to pre-COVID-19 levels. Investor optimism regarding the EU's recovery fund and Fitch's confirmation of Spain's rating (A–) also helped in this regard. The yield curves of lower-risk debt such as that of the US and Germany, meanwhile, remained relatively stable in the face of the rise in uncertainty regarding the economic outlook towards the end of the month. In this context, the US dollar weakened against most advanced currencies and the euro stood above 1.12 dollars.

Central bank balance sheets as a percentage of GDP

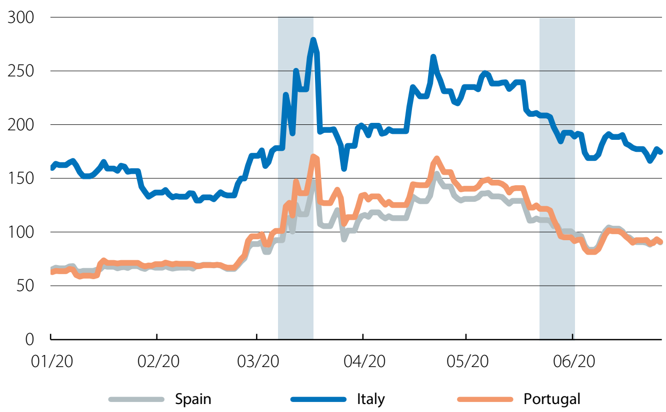
(%)



Source: *CaixaBank Research, based on data from Bloomberg.*

Euro area: risk premiums of 10-year public debt

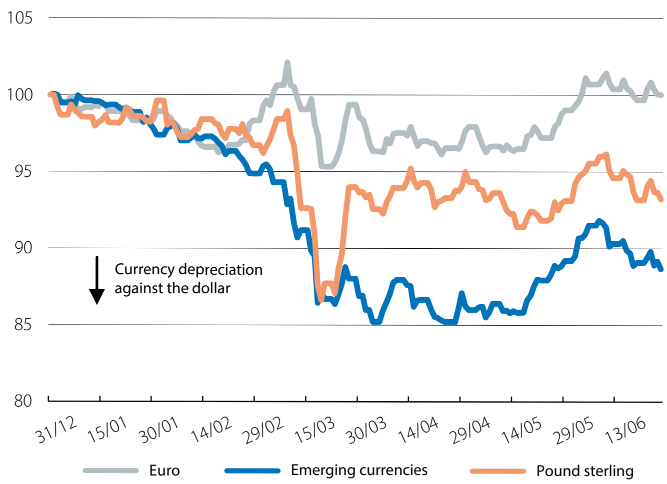
(bps)



Note: *The shaded areas indicate, from left to right, the spread of COVID-19 in March and the EU's Recovery Fund proposal in May.*
Source: *CaixaBank Research, based on data from Bloomberg.*

International currencies against the dollar

Index (100 = January 2020)



Source: *CaixaBank Research, based on data from Bloomberg.*