



**Market Outlook – Why Have Markets Recovered in a Recession?**  
**September 2020**

**Summary**

Although markets look expensive on short term forward earnings multiples, it is the valuation change that has driven equity returns in 2020. There has been a collapse in real yields, interest rates and fixed returns. Investors are even prepared to lock themselves into 10 year US inflation linked bonds at negative real return of -1%, and in this context equities have become the TINA (There Is No Alternative) asset class for investors looking for a return ahead of inflation. Investors have underestimated the impact of low yields on stock market multiples and even for the strongly performing technology giants, their earnings yield when taking into account the 10 year treasury yield, look attractive. The current earnings yield on the S&P 500 at around 3.8% is around 3% higher than the 10 year Treasury yield and compared to bonds US equities are still not expensively priced.

The markets have clearly been saying for a while that the economics of the post pandemic world will be different. In some instances it seems some businesses and practices have leapt forward more than a decade. Central bank largesse in tightening credit spreads have helped equity markets and as noted in previous commentaries this environment is rarely negative for investors. Covid-19 has altered the prospects for many sectors in very different ways: homeworking, home schooling, home entertainment have all benefitted technology names whilst home eating has boosted food delivery stocks. The trend to home shopping has further accelerated. Markets are forward looking and the progress to date both on vaccine trials and improved treatments continue to allow markets to look across the valley to the better times of 2021 and 2022. Covid-19 will not see a recovery across all sectors and disruption means the process of creative destruction, written about by Joseph Schumpeter, economist, has polarised the world of winners and losers to a greater degree than many investors will heretofore have experienced.

