FlatRock Associates

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Are markets more immune than humans?

It seems that the equity market is immune from a lot of ailments unlike humans.

Rising geopolitical tensions, surging unemployment, crumbling growth, and widespread social unrest are doing little to rattle equity markets in the US. Investors all over the world have generally been on edge since late March because fundamental economic data does not exactly point to such market levels. The market's immunity from all the turmoil is mind-boggling to analysts, investors, and regulators (or maybe not to the latter as I will explain later). This begs the question: Who is buying?

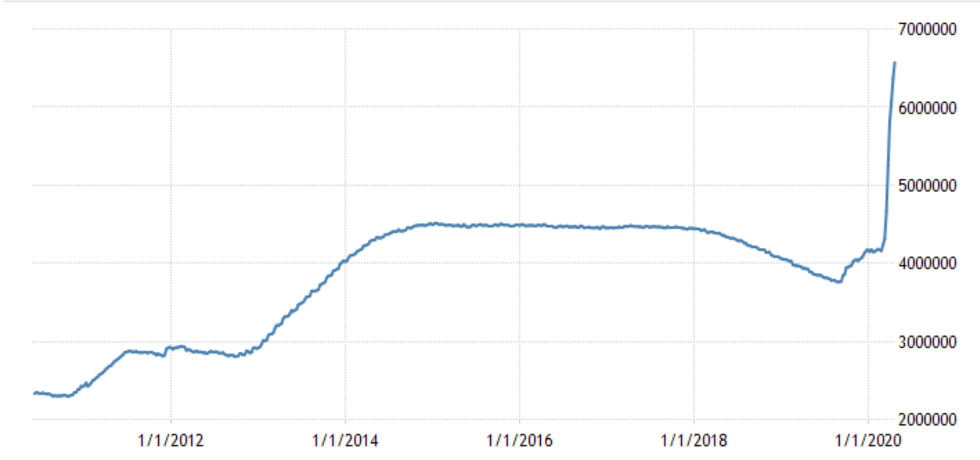
Corporate buybacks are not pulling equities upwards.

Perhaps corporate buybacks can explain what is going on. However, since there has been a lot of negative sentiment surrounding buybacks because corporations mainly use this tool to pump up share prices, I doubt this is making stocks bullish. On top of that since profits have been slumping since the end of Q1 companies are burning through cash just to keep the lights on (well most of them anyway).

Now I am not going to waste your time trying to explain why I don't think that institutional investors are purely behind the bullish sentiment especially if you have been reading the research that is being churned out by the largest investment banks like Goldman Sachs who up until a few days were underweighting equities. They may be behind the rally **solely** because of the Fed's actions.

This rally is clearly stimulated by the Fed's actions.

In March, the US Federal Reserve rolled out some heavy weaponry to deal with the "nuclear" fallout of the pandemic-induced lockdowns. They essentially put the economy on a ventilator and pumped liquidity into the system by rapidly expanding their balance sheet. Taking the risk off the private sector's balance sheets, the Fed "encouraged" institutional investors to turn towards stocks. As long as there is no imminent threat from runaway inflation, the central bank will keep on injecting liquidity into the system which has led many analysts to call this a TINA (there is no alternative) moment.



Source: *US Federal Reserve*

Caution is still advised because there is only so far markets can go before economic reality begins to set in. Until now there has been no spike in cases but it could all go south very quickly. Also, I was inclined to believe that maybe individual investors also had a hand in this rally probably because they wanted to get in on the action but that does not seem very likely. If there are adding fuel, then there is that fear that another bubble could be inflating.

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