A moment in markets – Is all the vaccine good news priced in?

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Are uncertain future outcomes ever fully priced in? Is it even possible to foresee a world where we have a combination of future outcomes being absolutely certain, and markets being perfectly efficient in translating that certainty into prices?

Neither holds true in the world we live in. The future is inevitably uncertain even when a posited scenario seems highly likely; and perfect market efficiency does not exist. At best, sophisticated markets have a semi-strong form of efficiency; they price in publicly available information at that moment in time.

The rollout of the vaccine worldwide and its impact, along with everything else that might happen in the world next year, remain uncertain variables. Therefore, if all the vaccine good news is not priced in, what could move markets in 2021?

Potential avenues of 'good news'

Going into 2021, the following forces may act as tailwinds for equity markets:

1. Economic growth: As of the end of Q3, advanced economies – including the US and Eurozone – are yet to recoup their losses from earlier in the year. If an effective administration of vaccines puts an end to the pandemic worldwide, the global economy could return to a steady state of growth.

2. Accommodative monetary policy: Major central banks including the US Federal Reserve (Fed) and the European Central Bank (ECB) are expected to remain accommodative in the year ahead – particularly the Fed which will most likely allow inflation to run above its usual 2% target for longer. Let's not forget, accommodative monetary policy has been a key driver of equity markets since the global financial crisis.

3. Fiscal stimulus: If vaccines are fully successful, they will help eliminate the pandemic problem. That doesn't automatically translate into growth – something governments will be looking to contribute towards. Central banks have recently been echoing a voice of caution on economic growth. Both the Fed and the ECB have emphasized the need for fiscal stimulus to support the already accommodative monetary policy and to give economies the impetus to start firing on all cylinders again.

4. Pent up demand: Economic growth stalled this year because many people were forced to forego holidays, were unable to make those trips to the theatre and decided not to buy those clothes and shoes they would

have otherwise had they been socialising as normal. Economists argue this creates ‘pent up demand’ and people are likely to spend more when they can next year. More holidays and longer stays?

5. Brexit clarity: As of 11 December, UK’s FTSE 100 is still down over 13% (in Sterling terms). While the pandemic has had a devastating impact on the UK economy this year, it is difficult to disregard Brexit uncertainty as playing a part in holding UK equities back from rallying. UK and European markets will welcome clarity on this front in the year ahead.

6. Steady trade policy: Could markets expect a more stable approach to policy action from the US under Joe Biden relative to the current administration? What is true is that markets detest surprise disruptions to the flow of capital. A more stable and coordinated approach from the US on its global economic policy – particularly as it relates to trade with Europe and China – is likely to be well-received by markets.

So, what could the impact be on equity markets?

A larger pie?

The global equity markets pie shrank in the first quarter of this year before regaining its size and eventually getting bigger than ever (the MSCI All Country World Index is up around 12% year-to-date in USD terms as of 11 December). The composition of the pie, however, changed with some markets (like the US) and sectors (like technology) acquiring a larger share while others, like Europe in terms of geography and financials in terms of sector, becoming smaller. In the year ahead, it is possible that not only does the pie grow further, it experiences some normalisation in terms of the composition with distressed sectors and markets playing catch-up.

The key takeaway for investors

There are lots of things that could move equity markets in 2021 – some postulated in the list above and many that might come as surprises. A lot seems likely, but plenty remains uncertain. At WisdomTree, we endorse the notion of a high-quality core equity exposure complemented by targeted growth opportunities – particularly those in the thematic spaces like cloud computing, artificial intelligence and clean energy, among others. Sectors built on innovation will remain exciting as markets can never fully price in their growth potential – for innovation is, by definition, new and something that stimulates growth.

There is much to look forward to in 2021.

Source: All data sourced from Bloomberg as of 11 December 2020.

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