Markets Update: The Bull Run in 2021

JAKE SIEWERT: Welcome to our Exchanges at Goldman Sachs markets update for Friday, November 20th. Each week we check in with a leader across the firm to get a quick take on what they're watching in the markets. I'm Jake Siewert, Global Head of Corporate Communications here at the firm. And my guest today is Peter Oppenheimer, Chief Global Equity Strategist and Head of Macro Research in Europe. Peter and his Goldman Sachs Research team are out with a new report titled "Global Strategy Outlook: The Bold Run in 2021." We'll be talking about that report today.

Peter, welcome back to the program.

PETER OPPENHEIMER: Thank you Jake. Great to be here.

JAKE SIEWERT: It's nice to see you with that sunny, London backdrop. What's your latest global growth outlook for 2021?

PETER OPPENHEIMER: Well, from the title of that outlook piece we did, you know, we are optimistic, both for equity markets, risk assets, and, indeed, the economy. If we look at the economy first of all, we're forecasting global growth next year of 6 percent. And that's quite a bit above the current consensus, which is a little bit more than 5 percent. We're well above consensus for the US. We're looking at around 5.3 percent growth there. And pretty much the same across Europe. So, a strong economic recovery, albeit from a very low base, one of the deepest recessions, of course, that we've had for many decades. But I think that this strong outlook is supported by the prospects for more positive news on vaccines and the implementation of those, as well as very, very supportive monetary and fiscal policy through the course of next year.

JAKE SIEWERT: So, a lot of the attention in the States has been around fiscal stimulus and what we can expect. For the US, what kind of fiscal stimulus are you modeling? And what does that mean for your economic growth forecast?

PETER OPPENHEIMER: Well, our US economists are expecting most probably a fiscal boost of about a trillion dollars. Probably late this year or if not early next year. That does, of course, depend a little bit on the final outcome in terms of the Senate and what happens in Georgia. If there were a Democratic lead in the Senate as well, the scale of that fiscal boost would likely be ultimately in excess of $2 trillion. So, it will depend a little bit on that.

In the initial period after the election, there was some concerns in the market about the potential for a fiscal boost to be scaled down. But on the other hand, we do still expect fiscal support to come through. And perhaps less risk of rapidly rising taxation. So, overall that would support growth in the US economy of about 5.3 percent for next year.

Another important point to mention about the US is that savings rates have increased quite sharply through the pandemic as people have, of course, been spending less and generous employment supports have kept incomes continuing to be reasonably good overall. So, there's a lot of pent up demand and savings power to support quite a strong consumer recovery. So, the winter months are likely to be difficult in the US and elsewhere given rising infection rates. But from the second quarter onwards we've been expecting to see 7 percent and then 6 percent annualized growth in the second and third quarters in the US. So, quite a strong rebound, particularly in the second half of the year.

JAKE SIEWERT: Well, yes, hopefully we'll have some things to spend money on: travel and the like, as we escape the paradox of thrift. So, there's a lot of debate around what the bear market looks like. I mean, most people think COVID was an event-driven bear market, which is very different than a cyclical or structural downturn. How does that factor into what you're seeing around the pace of both, what we saw in the pace of the collapse and the pace of recovery?

PETER OPPENHEIMER: Yeah, that's a very good point, Jake, because as we all know the speed of the initial collapse into bear market territory as the pandemic took hold was the fastest downturn that we've seen in most market cycles since 1929. But then again, the rebound from the March low has been the most rapid we've seen, again, since actually the period coming out of the 1929 crisis. So, very, very V shaped.

I think there are two reasons for that. The first one is the very unusual nature of this recession. Now, this recession has been very, very deep. But as you say, it wasn't really triggered by economic factors like rising inflation or rising interest rates or collapsing asset prices like many recessions are. It was actually triggered by an exogenous shock, the pandemic, which derailed the economic cycle. And was really forced on economies by government policies to constrain mobility. But as those mobility rates start to improve, particularly with a vaccine, we would expect to see a very rapid rebound.

The second factor is that this crisis has been matched by extraordinarily supportive policies, both monetary policy and as well very generous fiscal expansion. And that combination has gone a long way to reduce the potential structural damage to economies in the downturn by giving investors confidence that we can get out of this in relatively short period of time. And that also helped the rapid speed of the rebound we've seen.

But also, finally, just worth noting that in our view, central banks are likely to keep interest rates at these current levels, in most places around zero, well into 2025. And that means you've got a backdrop of extraordinarily low interest rates, actually negative real interest rates. And that should be quite supportive for risk assets like equities.

JAKE SIEWERT: So, you have a great phrase in the report. You talk about moving from the hope-driven phase of the bull market to the growth-driven phase. Explain what a hope-driven phase markets is. And I think we understand what a growth-driven phase is. But explain why you think that transitions in the [UNINTEL]?

PETER OPPENHEIMER: Yeah, absolutely. Well, we've done a lot of work looking at historical cycles going back over a couple of centuries. And equity cycles, of course, vary in length and strength. But they do tend to exhibit different phases, which are driven by different factors, sometimes prices arising as valuations go up. Sometimes as earnings go up. And on occasion, of course, you get prices falling in anticipation of declining earnings. That's really the bear phase or the despair phase, as we call it.

But the hope phase is what we describe as the initial phase of a new bull market. Now these nearly always start during recessions when profits are still falling. And for some reason investors start to get optimistic about a future recovery. And that phase, that hope phase tends to be very strong, but almost entirely driven by risings valuations because earnings are still negative. And that's really what we've seen, we think, between March and October of this year. Deep recession. Profits were falling. But as infection rates slowed in the summer and this very supportive policy came through, we got that very rapid hope-driven acceleration in equity markets. And we think we're moving into what we call the growth phase, which is the longest part of a bull market, where most of the profit growth and the dividend growth tends to emerging.

And the transition between those two often is associated with high volatility. We've seen that recently. And we think this growth phase is emerging because next year we're looking at global profit growth to be around 35 percent. Now albeit, that's from a big fall this year, about 20 percent. But that recovery in profits, we think will come through and put us into that longer phase of growth in the equity bull market cycle where returns will probably be lower, and valuations will probably start coming down a bit.

JAKE SIEWERT: So, one of the interesting things about the recovery markets is that it hasn't been widely dispersed. But will the rally you're projecting in 2021 be evident across all equities? Or will certain categories or sectors be left behind?

PETER OPPENHEIMER: Yeah, that's a great question. I think it's worth mentioning the context. You know, one of the really dramatic things that we saw in the decade or so after the financial crisis is the huge out performance of the US equity market, many others got left behind. And also the significant out performance of growth type equities, whereas value, cheaper equities and often more cyclical companies, also underperformed. Now, why did that happen? It happened really because we went into a decade of very low growth and low profitability, which meant that people were paying for growth. Secondly, the interest rates were incredibly low, and that boosted the valuations attributed to very long duration assets, growth assets. And thirdly, because we saw tremendous success and out performance of the technology industry, which was much more profitable than most others. And of course, that explained the out performance of the US. The US had a much bigger weighting, a much bigger exposure to these high growing parts of market.

And as we move forward in time, we do expect to see more even returns globally. Less sort of an extreme out performance of the US. We would expect people to be diversifying more by country, region, and by industry. We've also argued in recent weeks that some of the underperforming, more economically sensitive industries and value-type parts of the market should also rebound as you move into an inflection point of much stronger growth with slightly rising inflation expectations backed by this policy support that we've discussed.

So, I think 2021 should be a year of pretty good returns overall, but ones which are more evenly distributed both geographically and across industry.

JAKE SIEWERT: All right, well Peter, we look forward to a happier new year. Thanks for joining us today. And we look forward to seeing you in 2021.

PETER OPPENHEIMER: Thank you, Jake.

JAKE SIEWERT: That's all for this week's markets update on Exchanges at Goldman Sachs. And in case you missed it, check out our other episode this weak on the economy in Germany with Wolfgang Fink, CEO of Goldman Sachs Germany and Austria.

Thank you for listening and hope everyone has a great weekend. This podcast was recorded on Thursday, November 19th, 2020.