

Risk Appetite—For Now—It’s the Only Game in Town

Impressive back to back gains for the US equity markets, taking the S&P 500 some 16% off Monday’s low, have prompted a broad sigh of figurative relief in markets—sending volatility lower, undercutting FX safe havens and lifting the high beta currencies. It would be nice to think that the worst is over but it’s really too soon to say—we can only call the definitive low for stock markets with the benefit of (a lot of) hindsight. Risk currencies can firm a little more in the short run we think but scope for broader gains is less certain—and more likely limited for now.

As bear markets go the February/March swoon in the S&P 500 has been brutally quick but remarkably average in terms of its scale. The index peeled off 35% in value in just 25 days from the February high to the March 23rd low, compared with the average length of bear markets since the 1980 of 336 days. However, the 35% decline puts it bang on the average decline in the index in bear markets over that period. That will cheer anyone looking for a low point in equity markets but it’s not clear—and probably won’t be for some time—that the low is in at this point. A new bull market phase—where the previous high is surpassed rather than markets simply making a gain of more than 20%—is still further away.

Optimists will note that this is not a typical economic downturn, rather a sudden stop amid otherwise healthy fundamentals which former Fed Chairman Ben Bernanke likened to a natural disaster—albeit a severe one—rather than a depression. The rebound from a sharp contraction in global output is expected to be relatively rapid. Moreover, the combined level of fiscal and monetary policy support provided by the global authorities has been impressive—and more may come. This will provide a significant backstop for risk assets in the coming months. Finally, margin calls and forced selling of assets appears to have abated; central banks have stepped up to ensure ample market liquidity is at hand, even if there are signs that global banking systems’ “plumbing” is still backed up a little in some areas. Looking at what is right about an “average” haircut for stocks in recent downturns, bargain hunters have been active.

If the past really is any sort of guide, it should also be apparent that marking the low point for stock market downturns is not an obvious exercise. No one rings the bell at the top—or the bottom—of markets. Since the 1980s, equity market recoveries have typically been pretty slow and pretty messy in developing. Average gains following the low point for the bear markets noted above, right are 30% six months after the low but are more typically a little more than 20%. A high close for stocks this week will bolster expectations for additional gains in the short run because technicals will look compelling. But we might already have seen half or three quarters of the gains we might expect to emerge through the Oct/Nov period already.

There are a number of risks that can easily derail optimism. How well the Western economies manage (or not) the virus is one risk, the re-emergence of cases in China as the lockdown there ends is another. Economic expectations appear suitably subdued for the near-term and a lot of bad news is probably factored into market thinking now. But weaker than expected data or a more persistent slowdown that limits forward visibility on earnings even further will curb the ability for stocks to rebound.

Unfortunately, for the FX markets, equity market trends and volatility are likely to remain the primary driver of market movements for the next few months at least. All

 FOLLOW US ON TWITTER [@SCOTIABANKFX](https://twitter.com/SCOTIABANKFX)

Shaun Osborne
Chief FX Strategist
416.945.4538
shaun.osborne@scotiabank.com

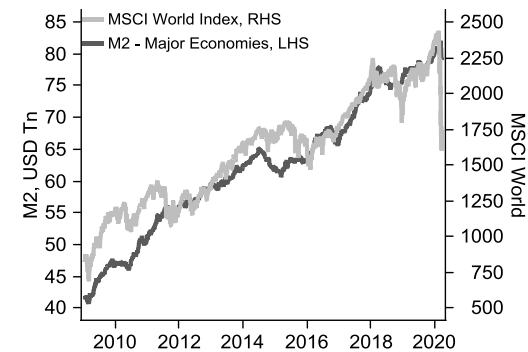
Juan Manuel Herrera
FX Strategist
416.866.6781
juanmanuel.herrera@scotiabank.com

S&P 500 Bear Markets Since 1980

Date	Pct Decline	Days
1980/82	-27	622
1987	-34	101
2000/01	-37	546
2002	-34	278
2007/08	-52	408
2009	-28	62
Avg	-35	336
2020	-35	25

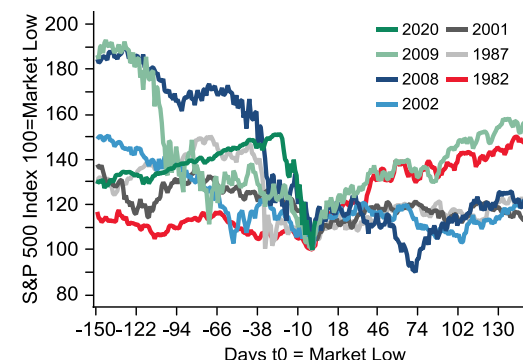
Source: Scotiabank FICC Strategy calculations

Central Bank Liquidity Backstops Risk



Source: Macrobond, Scotiabank FICC Strategy

How Bear Markets End



Source: Macrobond, Scotiabank FICC Strategy

major economies are similarly positioned now and all major central banks are more or less on the same page (we assume the Bank of Canada will cut another 50bps in the coming weeks), making fundamental differentiation less obvious than usual.

That likely means a window for commodity FX to gain a little more ground in the short run while the JPY and CHF should remain better supported on dips in the medium term because there will be bumps and setbacks in the recovery process even if everything goes well. We think the USD's role as a haven will diminish as dollar funding pressures ease amid a flood of central bank liquidity aimed precisely at easing offshore funding demand.

IMPORTANT NOTICE and DISCLAIMER:

This report is prepared by Scotiabank as a resource for clients of Scotiabank for information and discussion purposes only. This report should be considered a marketing communication and has not been prepared by a member of the research department of Scotiabank, it is solely for the use of sophisticated institutional investors, and this report does not constitute investment advice or any personal recommendation to invest in a financial instrument or "investment research" as defined by the UK Prudential Regulation Authority or UK Financial Conduct Authority. This document has not been prepared in accordance with EU legal requirements designed to promote the independence of investment research and the information contained in this publication is not subject to any prohibition in the EU on dealing ahead of the dissemination of investment research. Opinions, estimates and projections contained herein are our own as of the date hereof and are subject to change without notice. The information and opinions contained herein have been compiled or arrived at from publically available sources believed reliable but no representation or warranty, express or implied, is made as to their accuracy or completeness and neither the information nor the forecast shall be taken as a representation for which Scotiabank or any of its employees incur any responsibility. Neither Scotiabank nor its representatives accept any liability whatsoever for any loss arising from any use of this report or its contents. This report is not, and is not constructed as, an offer to sell or solicitation of any offer to buy any financial instruments and has no regard to the specific investment objectives, financial situation or particular needs of any recipient. It is not intended to provide legal, tax, accounting or other advice. Scotiabank and/or its respective officers, directors or employees may from time to time take positions in the products mentioned herein as principal or agent. Directors, officers or employees of Scotiabank may serve as directors of corporations referred to herein. Scotiabank may have acted as financial advisor and/or underwriter for certain of the corporations mentioned herein and may have received and may receive remuneration for same. This report may include forward-looking statements about the objectives and strategies of Scotiabank. Such forward-looking statements are inherently subject to uncertainties beyond the control of Scotiabank including but not limited to economic and financial conditions globally, regulatory development in Canada and elsewhere, technological developments and competition. The reader is cautioned that the member's actual performance could differ materially from such forward-looking statements. Past performance or simulated past performance is not a reliable indicator of future results. Forecasts are not a reliable indicator of future performance. You should note that the manner in which you implement any of strategies set out in this report may expose you to significant risk and you should carefully consider your ability to bear such risks through consultation with your legal, accounting and other advisors. Information in this report regarding services and products of Scotiabank is applicable only in jurisdictions where such services and products may lawfully be offered for sale and is void where prohibited by law. If you access this report from outside of Canada, you are responsible for compliance with local, national and international laws. Not all products and services are available across Canada or in all countries. All Scotiabank products and services are subject to the terms of applicable agreements. This report and all information, opinions and conclusions contained in it are protected by copyright. This report may not be reproduced in whole or in part, or referred to in any manner whatsoever nor may the information, opinions and conclusions contained in it be referred to without in each case the prior express consent of Scotiabank. Scotiabank is a Canadian chartered bank.

If you are affected by MIFID II, you must advise us in writing at trade.supervision@scotiabank.com.

TMTrademark of The Bank of Nova Scotia. Used under license, where applicable. Scotiabank, together with "Global Banking and Markets", is a marketing name for the global corporate and investment banking and capital markets businesses of The Bank of Nova Scotia and certain of its affiliates in the countries where they operate, including, Scotia Capital Inc. and Scotia Capital (USA) Inc., Scotiabank Europe plc, Scotiabank (Ireland) Limited - all members of the Scotia-bank Group and authorized users of the mark. The Bank of Nova Scotia is incorporated in Canada with limited liability. Scotia Capital Inc. is a member of the Canadian Investor Protection Fund. Scotia Capital (USA) Inc. is a broker-dealer registered with the SEC and is a member of FINRA, NYSE, NFA and SIPC. The Bank of Nova Scotia is authorized and regulated by the Office of the Superintendent of Financial Institutions in Canada. The Bank of Nova Scotia is authorized by the Prudential Regulation Authority and subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. Details about the extent of The Bank of Nova Scotia's regulation by the Prudential Regulation Authority are available from us on request. Scotiabank Europe plc is authorized by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority.

To unsubscribe from receiving further Commercial Electronic Messages click this link: www.unsubscribe.gbm.scotiabank.com.