# A year after Covid-19, capital markets are in uncharted waters

CFA Institute's survey report, *Covid-19, one year later,* shows that equity markets are perceived to have progressed out-of-pace with the real economy as a result of monetary stimulus. PHOTO: AFP

**By Olivier Fines**

WITH the Covid-19 crisis, capital markets have entered uncharted waters. Indeed, the role of finance in society could be materially changing. CFA Institute conducted a survey of its global membership to analyse the effects of the Covid-induced economic crisis on financial markets and the investment industry. The survey was run worldwide from March 8 to 28, 2021. Now we are releasing the survey report: *Covid-19, one year later.*

This research constitutes the second iteration of our work on the effects of the Covid-19 crisis. The first survey results were released in June 2020, and were based on a worldwide survey conducted from April 14 to 24, 2020.

The 2020 crisis marked an unprecedented event in the history of economic and financial crises. While economic lockdowns were implemented in response to the health emergency, public authorities resorted to a novel approach to bridge the gap for economic actors until the recovery would kick in.

For the first time, governments and monetary authorities in advanced economies agreed to coordinate fiscal policy and monetary policy as a combined response to the economic crisis that would ensue. The objective has been to preempt any direct transmission of the crisis into financial markets and to avoid a similar dislocation of credit and money markets at the core of the 2007-2009 Global Financial Crisis.

Our research reviewed how such a transformational interpretation of the role of central banks and their independence in conducting monetary policy could have unintended consequences for financial markets and the economy.

CFA Institute also wanted to draw the attention of policy makers to the socioeconomic aspects of this crisis. As part of our analysis, we reviewed how the recovery may be affecting various parts of the economy in materially different ways, depending on regions, industries, and social categories under consideration. The fragile equilibrium among the various economic stratums of society may be affected by these stimulus measures.

We structured our study of the survey results around a series of nine analytical themes or sequential stories, which the full report explores with granularity and contextualisation. The survey results are complemented by our market analytics and economic research. Those themes were as follows:

### The shape of the economic recovery

One year after the start of the crisis, the recovery that is forming could be taking a K-shape, in which different parts of the economy, markets, and social categories are affected in materially different ways.

■ Key survey result: A plurality of 44 per cent of respondents globally see the economy of their region recovering in the form of a K-shape, which is an economic course that affects different categories of people, businesses, regions, and industries in varying ways.

### Equity markets and the real economy

We show that equity markets are perceived to have progressed out-of-pace with the real economy as a result of monetary stimulus.

■ Key survey result: A plurality of respondents globally expressed the view that equities in their respective markets (45 per cent) and global developed markets in general (43 per cent) have recovered too quickly from the market slump in February-March 2020 and are due for a correction within the next one to three years.

### Inflation may be back on the agenda

Input prices have been the first to show nervousness in connection with the output gap generated by the crisis. The question will be whether this is temporary or structural.

■ Key survey result: A large majority or 65 per cent of respondents globally believe that an accommodative monetary policy combined with supply-side constraints will cause inflationary pressures over the next one to three years. Those respondents, however, appear to be split equally on whether this inflation will cause central banks to restrict monetary policy as a result (31 per cent think central banks will switch to a restrictive policy and 34 per cent think not).

### Structural consequences of the crisis on the economy

We may be observing structural transformations to the traditional economic balance, with the rise of central bank interventions and a larger role for governments, Big Tech as the clear winners, and environmental, social, and governance issues (ESG) as a forceful trend in financial services.

■ Key survey result: At a global level, 58 per cent of respondents agree that the role of government will broaden as a result of the crisis and that the share of government spending in GDP will structurally and materially rise, as will taxes. In addition, 40 per cent agree that the Build Back Better movement and the trend towards sustainable investment products are structurally strong.

### The financing of economic relief programmes

How the government economic relief programmes will be paid for is a key question with taxes and debt monetisation under consideration.

■ Key survey result: A large majority of 65 per cent of respondents believe there will be a rise in the general level of taxation to finance government economic relief programmes.

### Monetary stimulus by central banks

The question should now switch to whether it will be possible to normalise monetary policy while authorities are wondering how to coordinate money supply and fiscal policy.

■ Key survey result: At a global level, respondents are split on whether the current extraordinary cycle of accommodative monetary policy should start being restricted (51 per cent) or whether it should continue to support people and businesses until the economy is sufficiently stable (43 per cent).

On the question of the importance of central bank independence, 35 per cent would support a coordination of monetary and fiscal policy, whereas 29 per cent think it is a bad idea because central banks should operate independently from the Treasury.

### Socioeconomic consequences of stimulus measures

Authorities should consider the effects of economic and monetary stimulus on the fragile balance among the various socioeconomic stratums.

■ Key survey result: At a global level, 44 per cent of respondents believe the stimulus measures have created a goldmine for the investor class, widening the wealth gap with the working class.

### Regulators and the crisis

Regulators fared well during the crisis, but a key question now is about the major risks they should be focusing on.

■ Key survey result: Globally, a majority of respondents (51 per cent) agree that regulators have overall properly addressed the situation in line with their mandate. On the question of key risks regulators should now focus on, 40 per cent agree that systemic risk and "too-big-to-fail" institutions in risk of distress should be a concern for regulators.

### Corporates

In the short-term, it would appear that the risk of corporate credit default risk is on the rise, but it could normalise over the longer term. In the meantime, corporates should provide investors with more forward-looking information to enable them to assess the impact of the crisis more precisely.

■ Key survey result: A majority of 56 per cent of respondents globally think credit default risk has increased in the short term (1-3 years), compared with 43 per cent who think so in the medium term (5 years) and 32 per cent over the long term (10 years), which may indicate that respondents expect the market to stabilise progressively.

On the question related to financial reporting priorities as we emerge from the crisis, 23 per cent of respondents agree that forward-looking information is the most important aspect to focus on, to help assess the impact of the crisis on companies' anticipated results.

As these themes and statistics are analysed in the full report, we are drawing the attention of policymakers on what we think are key learning outcomes from the crisis. CFA Institute believes it is important to consider those factors to prepare for future crises more efficiently. One important lesson from the 2020 crisis is the extent to which it is difficult to craft one-size-fits-all public policies.

Potential unintended consequences may materialise from these policies, which need to be carefully appreciated.

■ Olivier Fines, CFA, is head of Advocacy and Capital Markets Policy Research for EMEA at CFA Institute