

# Class 1: Financial Markets Amidst Covid-19

Financial Markets, Spring 2021, SAIF

**Jun Pan**

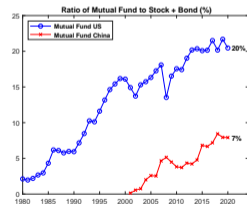
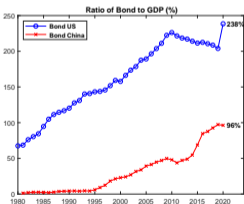
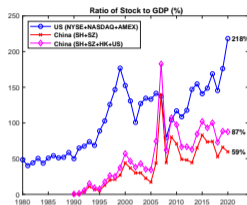
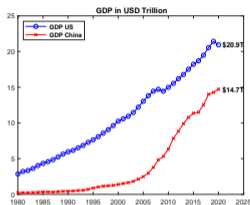
**Shanghai Advanced Institute of Finance (SAIF)  
Shanghai Jiao Tong University**

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# Outline

- During the current Covid-19 crisis, the price discovery function of financial markets becomes all the more important. Financial market should remain open for:
  - ▶ Timely aggregation and processing of otherwise diverse information.
  - ▶ Efficient allocation and distribution of capital and resources.
- Comparisons to past crises:
  - ▶ 1987: stock market crash.
  - ▶ 2008: financial crisis.
  - ▶ 2020: ?
- The politics of financial markets:
  - ▶ Central banks and governments: their respective responses and responsibilities.
  - ▶ Collisions of states' interests: an all-out war on oil price in 2020 amid Covid-19.

# Capital Markets in the US and Chinese Economy

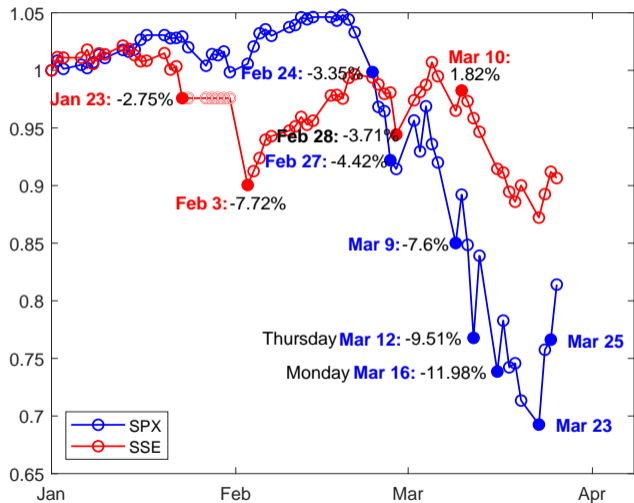


End-2019	US	CN
GDP	\$21.4T	\$14.3T
Equity	\$38T	\$13T
Bond	\$44T	\$14T
Mutual Fund	\$18T	\$2T*

End-2020	US	CN
GDP	\$20.9T	\$14.7T
Equity	\$46T	\$13T
Bond	\$50T	\$14T
Mutual Fund	\$20T	\$2T*

\* Includes money market funds

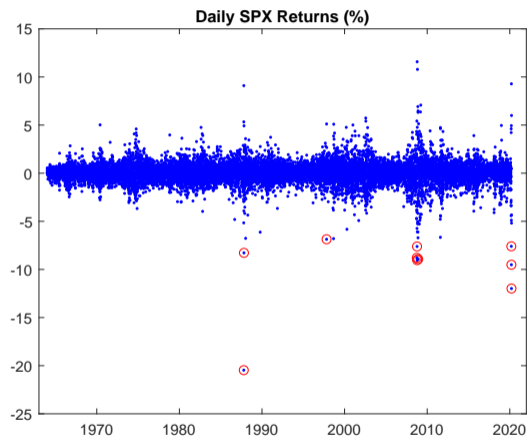
# Equity Markets' Reactions to Covid-19: US and China



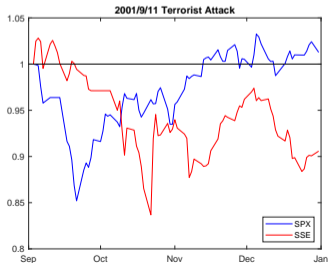
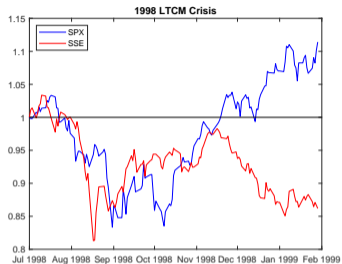
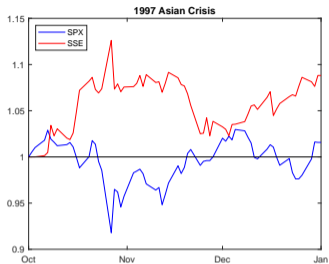
- 1/23: Wuhan lockdown.
- 2/04: Covid19 test approved by FDA.
- 2/12: CDC: Faulty virus tests.
- 2/24: Virus widely spread outside China.
- 2/25: Trump: USA under control.
- 2/26: Trump: Pence leads virus response.
- 2/27: CDC: test criteria revised.
- 3/03: Fed: rate cut by 50 bps.
- 3/10: President Xi visits Wuhan.
- 3/11: Trump: TV address.
- 3/12: Fed: injects \$1.5T via term repo.
- 3/13: Trump: national emergency.
- 3/15: Fed: rate to zero and \$700B QE.
- 3/17: Fed: CP funding & PD credit facility.
- 3/18: Fed: MMMF liquidity facility.
- 3/23: Fed: Infinite QE announced at 8 am.
- 3/25: Senate: \$2T relief bill passed 96-0.

## Top 10 Worst One-Day SPX Returns

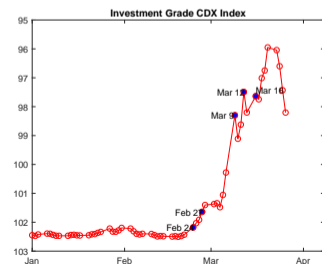
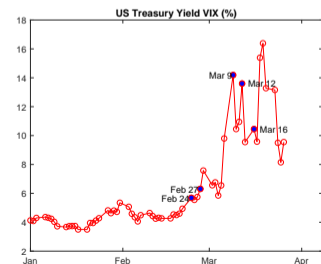
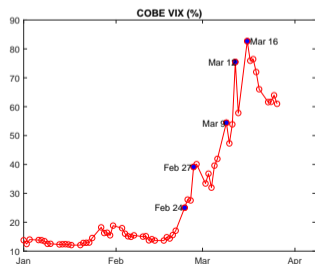
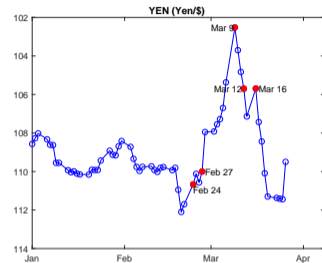
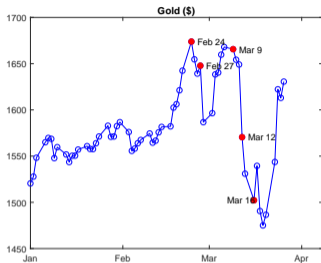
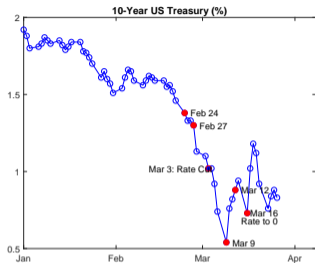
Rank		SPX Ret (%)	VIX (%)	SSE Ret (%)
1	10/19/1987	-20.47	150.19	
2	3/16/2020	-11.98	82.69	-3.40
3	3/12/2020	-9.51	75.47	-1.52
4	10/15/2008	-9.03	69.25	-1.12
5	12/1/2008	-8.93	68.51	1.25
6	9/29/2008	-8.79	46.72	0.00
7	10/26/1987	-8.28	113.33	
8	10/9/2008	-7.62	63.92	-0.84
9	3/9/2020	-7.60	54.46	-3.01
10	10/27/1997	-6.87	31.12	4.88



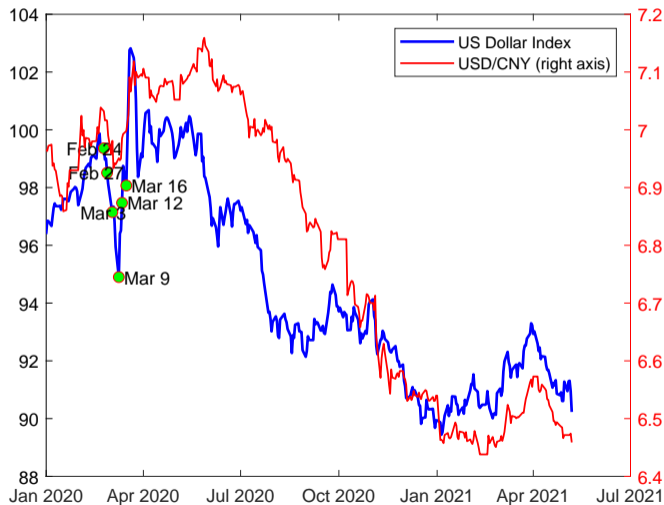
# Past Crises: SPX vs. SSE



# Traditional Safe Havens and Fear Gauges in 2020



# Dollar in 2020



**March:** the ultimate safe haven.

**Since June:** steady decline

- Uncertain path to recovery.
- Recovery elsewhere (e.g., China).
- Monetary policy:
  - ▶ zero short rate.
  - ▶ sub 1% 10-yr rate.
  - ▶ infinite QE injecting trillions of USD.
- Declining reserve holdings by foreign central banks?



# The Main Takeaways

- Financial markets are the most efficient aggregators of information.
- The maturation of China's markets and their integration into the global markets:
  - ▶ The increasing correlation between the US and Chinese equity markets.
  - ▶ The Chinese yuan becoming a prime indicator of dollar's strength.
  - ▶ China's bond market (to be discussed later).
- Questions to be answered by next week's student presentations:
  - ▶ What is the value of China's equity market to global investors?
  - ▶ What are the risk and return?
  - ▶ For a global investor, what should be his/her optimal portfolio weight on China according to financial theory?