INVESTMENT COMMENTARY

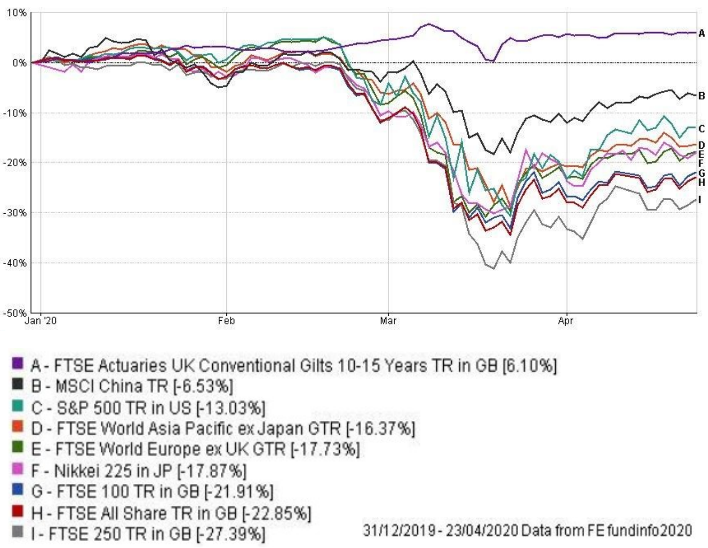
CARTLIDGE MORLAND

24 April 2020

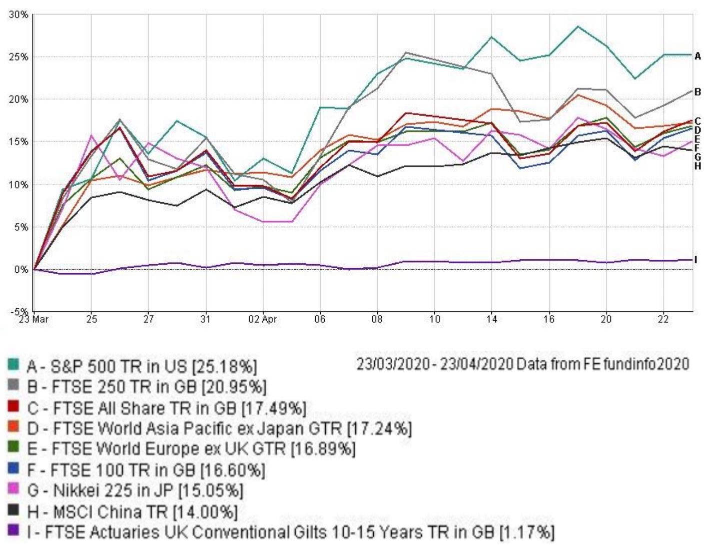
Over the past month, we have seen equity markets recover from their March 2020 lows following the seismic shock experienced in February, when the potential impact of COVID-19 on human lives and economies was realised. Gradually, investor sentiment has improved as central banks and governments globally have intervened and continue to do so in unprecedented ways to support the welfare of citizens medically and economically. Each day more is understood about the virus, as knowledge is shared globally, so doctors and scientists can improve treatment moving towards more helpful testing, vaccine development and perhaps a cure. The containment of the spread of the disease is being achieved through draconian measures, leading to a gradual fall in the mortality rate. This more reassuring backdrop supports more positive investor sentiment.

Investment Market Returns in Local Currencies

Year to Date



Over One Month



The next challenges relate to how and when economies move out of lockdown. Undoubtedly, the lockdowns have reduced pressure on health services and reduced the number of deaths from the virus, but the damage on business activity is unprecedented. Economic statistics in the UK, US and Europe indicate that their respective manufacturing, services and construction sectors are contracting at record rates. Unemployment rates are climbing steeply even though many countries are furloughing workers. The US has seen 26m people file for unemployment benefit in the five weeks since lockdowns were announced.

Wuhan, the original epicentre of the virus, has moved out of lockdown on a gradual basis and other countries are now following as infection rates decline. Germany, Austria, Spain and Italy have all started to open their economies, but care is required so that a second wave of COVID-19 does not arise. As businesses reopen, economic data will reflect signs of growth but it is very unlikely that there will be a V-shaped recovery. The recovery is likely to be U-shaped with an elongated base. Cyclical stocks such as energy and financials are usually early beneficiaries of a recovery, but some may take longer to recover than others given the nature of the downturn. Banks will have to survive in a very low interest rate environment, perhaps for a relatively long period. The equity market will reward companies which can generate growth and pricing power over the longer term. These are likely to be the least indebted companies. Technology companies are likely to perform well as proximity-tracking apps on smart phones become necessities and artificial intelligence penetrates job sectors, for example. Some now regard tech stocks such as 'Apple' and 'Microsoft' as modern utilities, so essential to everyday life are their technologies, and in turn they generate stable core earnings streams.

As for company earnings, it is impossible to predict what to expect for the year, as all depends on how the virus and global economy progresses through the remainder of 2020. As discussed in our commentary of 17 April 2020, dividends are likely to be cut/abandoned as companies conserve cash.

Markets will also be affected by other COVID-19 related factors. We saw oil prices technically move into negative territory at the beginning of the week as supply outstripped demand with worries about how and where to store the excess. Oil heavy indices, such as the FTSE 100, fell relatively sharply as a result. Subsequently, the US has taken action to shut old wells and stop new projects to reduce output whilst other countries have also moved to decrease output earlier than required via a recent deal between oil producers (OPEC+). The oil price has recovered to some extent but it remains under intense pressure. As economies reopen, there should be higher demand for oil.

PATIENCE NOT PANIC

Substantial progress has been made in clawing back February/March portfolio losses – although most portfolios are still below last Summer's levels, particularly those from which income is being drawn. Markets might fall again if COVID-19 acquires fresh momentum or if lockdown appears likely to continue well beyond mid-summer.

Damage to companies, their balance sheets and future earnings prospects can only be guessed at now, and once known there will be both upside and downside surprises, which will influence the direction of markets for better and worse as they unfold. Presently, analysts are guessing, based on the information available to them. Pricing partly reflects that but also wider trading activity, which with trading volumes relatively thin, has a decisive if somewhat misleading influence on the immediate direction of prices.

Currently, investors and their advisers have insufficient information available to make radical decisions. The certainties are that lockdown will end and that the business environment will be better in the future than it is now. In that sense, forward prospects can only be better and until a range of matters are clarified, portfolios may require adjustment to take advantage of particular opportunities or in some cases to mitigate future risks. However, in overall terms, the best opportunities and the greatest areas of risk will only become apparent later so patience is required at this point.

As always if you have any concerns please contact your usual Cartlidge Morland Partner/Director/Consultant.

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