CARTLIDGE MORLAND

INDIVIDUAL WEALTH MANAGEMENT

INVESTMENTCOMMENTARY

15 MAY 2020

OVERVIEW

Equity markets are still up from around 15% (Europe) to 28% (US) from 23 March 2020 lows. The past week has seen falls although some countries are now slowly easing lockdown restrictions. It would now seem that thankfully infection rates are falling across Europe. London appears to be ahead of the rest of the UK with the fewest new cases. Brazil and Russia are currently the countries with increasing infection rates. Oil prices have continued to rise as the market appears to be showing signs of slowly rebalancing, as demand gradually increases as lockdowns ease and Saudi Arabia has pledged to cut production. Investor sentiment has been adversely affected by US anti-China rhetoric coupled with a warning from a US infectious disease expert that some US states may have re-opened their economies too quickly, risking a second wave of Covid-19 infections and the reintroduction of restrictions. The US dollar continues to be the supreme world currency, dealing a blow to the Chinese yuan. The US Federal Reserve has warned that the partial shutdown of the US economy is likely to lead to a recession and business failures on a "grand scale". Jay Powell, the Chair of the Fed, suggested that more fiscal and monetary support may be needed as a slower than hoped for recovery is anticipated. The shares of US Biotech and technology companies continue to perform well, so lending some support to the US equity market.

Chinese economic data points to how other economies may fare when they come out of lockdowns. Chinese industrial output figures have improved whilst vehicle sales are up 4.4% pa in April. Chinese inflation data is not as poor as forecast - consumer prices fell by 3.3% pa in April.

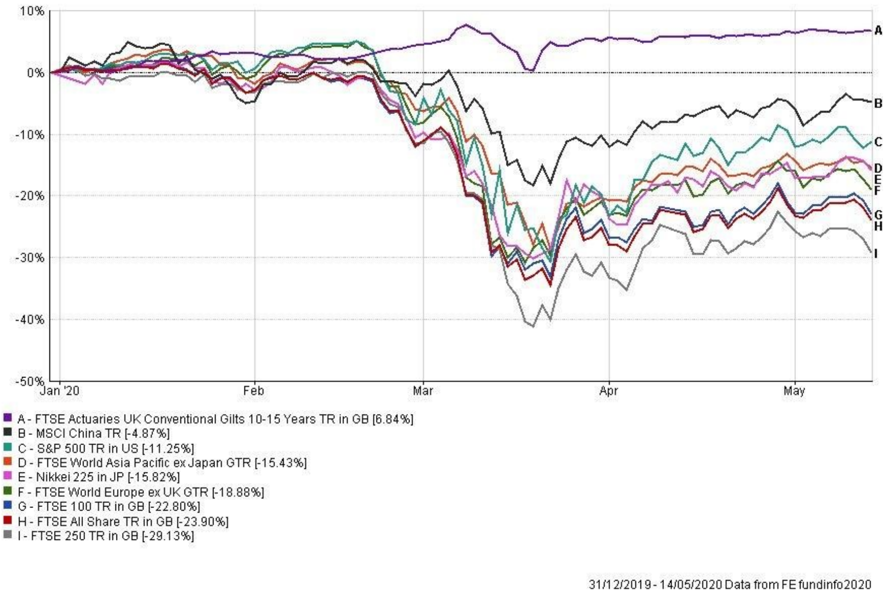
UK economic statistics are weak as expected. Retail sales fell by 19.1% pa in April although on-line spending was stronger. Credit card spending dropped dramatically over April. Against this weakening economic background, April's GDP figure is likely to be far worse than March's 5.8% fall. The second quarter figures are likely to be abysmal, but should improve in the third and fourth quarters as the economy slowly reopens and if there is no increase in the infection rate. The recent approval of an antibody test should support the easing of the lockdown. The Brexit negotiations continue, with the UK seeking a trade deal from the European Union which is similar to existing agreements with other countries such as Canada and South Korea. Tensions around these negotiations are likely to continue to impact negatively on the strength of sterling and domestic UK stocks already affected by the lockdown.

The European Central Bank (ECB) has indicated that the European economy hit the low point of the slump caused by actions to contain Covid-19 in April. There still appears to be a rift between the strong northern European economies such as Germany and the virus-weakened southern economies of Italy and Spain, for example. The German Constitutional Court has ruled that the ECB's support of these weaker economies in 2015 was unconstitutional, which impacts on current policy. The Italian government has passed a €50 bn stimulus package to support its economy, whilst the German economy continues to struggle - contracting 2.2% in the first quarter of 2020 - but has greater levels of state aid available to its companies. As many European economies slowly emerge from lockdowns there are fears about a second wave of infections which are likely to impact on investor confidence.

In fixed interest markets, there continues to be heavy bond issuance as companies look to rebuild their cash reserves. There is still high demand for longer-dated investment grade corporate bonds issued by stronger companies. Government bond yields are at near all-time lows as interest rate cuts, central bank asset purchase programmes and weak economic growth have pushed them lower. There appears to be little chance that interest rates will rise any time soon and there has been speculation that negative interest rates may be on the horizon for some central banks, which have been reluctant to adopt them to date. Negative interest rates in effect act as surcharges on excess deposits held by banks and other institutions at central banks and are designed to prompt lenders to offer more loans. The US Federal Reserve and the Bank of England are using other stimulus measures coupled with very low positive interest rates, rather than adopting negative rates.

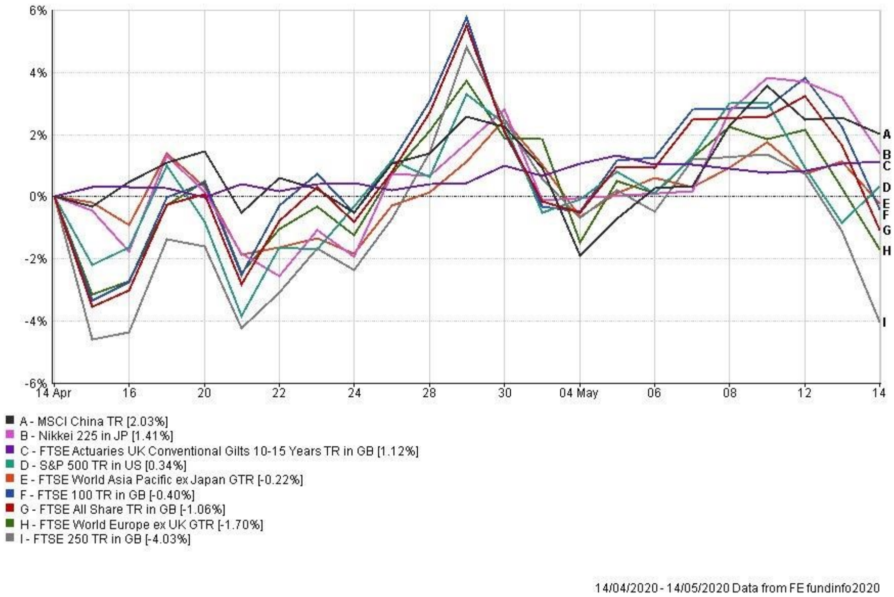
INVESTMENT MARKET RETURNS IN LOCAL CURRENCIES

YEAR TO DATE



INVESTMENT MARKET RETURNS IN LOCAL CURRENCIES

ONE MONTH



The key to investor confidence is how successful actions in easing lockdowns are. If economic activity picks up whilst the Covid-19 infection rate decreases and hopefully disappears, equity markets should increase too. Other non-virus related concerns may then begin to weigh more on markets. We continue to manage portfolios using a longer term view maintaining appropriate levels of risk in accordance with clients' risk tolerance and objectives. Profits from lower risk assets such as UK and international government bonds have been used to build cash positions where 'income' is required or topping up equity positions buying on equity market weakness. International equity positions have been added to so that portfolios are further diversified by geography and currency. Nevertheless, we retain lower risk assets to provide portfolio 'insurance' if markets become nervous as a result of increasing infection rates.

The CM Investment Commentary is compiled by Angela Cooper, Managing Director of Cartlidge Morland's Investment Services team.

Angela runs the firms' investment management propositions, with over 30 years' experience in investment research working for investment companies, leading UK national IFAs and wealth managers. Angela graduated from the London School of Economics and is a Chartered Insurance Practitioner.

LOOKING FORWARD

Investors and their wealth managers are facing a world that has abruptly changed. Whilst a broadly based 'U' shaped recovery appears most likely as lockdown eases globally, it is still too early to say what the medium term effect is on the outlook for sovereign debt (government bond issuance), the credit rating of corporate borrowers and the earnings of small, medium sized and larger companies globally. The latter affects corporate equity (share) and credit (bond) holders alike. There is much in principle to support the theory of burgeoning consumer demand supported by spending abstinence during lockdown, a high savings rate and consumers' desire to resume previous habits. The latter scenario would be favourable for those supplying goods/services in the large developed economies, in which consumer spending is the dominant component of GDP. This scenario undoubtedly holds an element of truth but to expect everything to return to how it was, is unrealistic.

As 'lockdown' is unprecedented, the predictability of consumer behaviour is less obvious. Consumers may be appreciating quieter lives and less financial pressure, as a consequence of spending less. Traditional expectations of consumers may prove outdated alongside 'consumerism'. People globally may look to simpler pleasures focussed on their families and homes. If so, this will be highly disadvantageous to the mature economies and to swathes of their businesses.

The slower, steadier recovery from 'lockdown' described above may prove disadvantageous to primary producers and developing economies too as customers in the developed economies would consume less. Conversely, it seems significantly less likely that appetite for voracious consumption will have declined amongst those still aspiring to achieve it. That will continue to support and expand demand for global brands and the luxury goods/services/ travel sectors.

Increasing talk of national 'happiness' or 'quality of life' indices in the developed economies suggest a potential change of mood which could increase the speed with which the fast developing Asian economies acquire per capita incomes closer to or even beyond Western/ Japanese levels.

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It is unlikely Western/Japanese populations will opt for a sustained 'quieter life' in which their nations become sleepily self-satisfied economic backwaters. It is more likely that should the trends suggested emerge as sustained themes (and they may not) then Western businesses will adjust to profitably satisfying the whims, requirements and demands of these changed societies. Efficient free market economies are equipped to respond quickly to changing conditions.

The recent oil glut and the plunge in the oil price provided a timely reminder that long-term, fossil fuel demand is likely to fall steadily and that the future is not reliant upon such fuels, any more than office computing turned out to be about once dominant 'Wang' or home entertainment 'Betamax', nor even video recorders. Technology and alternative energy sources are dominant investment themes, together with their further application across business, home, social and leisure activities. **There remain fortunes to be made and lost, so as always – diversification of risks and opportunities remain key.**

We are alert to the quickening pace of economic/societal change 'lockdown' is likely to bring and to the pivoting effect it will have on the type of goods/services in greatest demand. We are presently in the process of re-formulating our approach to accommodate these abruptly changed conditions for all that some long-held fundamentals will survive that change.

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

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