NLP Financial Management Ltd

Investment Team Update

5th May 2020

April has been another extraordinary month. The UK had entered a complete lockdown on 23rd March, with all but essential workers working from home for the foreseeable future, and Boris Johnson was admitted to intensive care. The disruption that the outbreak of COVID-19 has caused to the everyday lives of all of us is undisputable and will remain with us for some time yet. However, it seems the social distancing measures and the shielding of the vulnerable are working. It is becoming clear that we are past the worst of the infection, as Johnson announced 'We are past the peak. We are on the downward slope.' But governments will only be able to ease the lockdown measures gradually to prevent any new escalation in the infection rate. Several European countries have already set out their programmes detailing a series of phased steps to ease their lockdowns such as in Spain, Italy, Germany, Austria, and Ireland. The UK will announce its plan this weekend, including the possibility that primary schools will reopen and social distancing guidelines for businesses.

The crisis spilled over into financial markets as the economic impact of this pandemic became increasingly evident. The scale of the global shutdown is unprecedented as countries were plunged into a state of suspended animation. The key sectors hit hardest have been consumer-related areas such as leisure, restaurants, cafes, entertainment, tourism and travel. It has been unsurprising then that the data that came through towards the month end has confirmed the seismic impact on the economy. The US economy contracted by 4.8% compared to the figure last year, the UK was down -5.8%, and -3.8% for the Eurozone. These sorts of figures indicate a contraction not seen since the Second World War. Unemployment has risen sharply to over 2.3 million here and 30 million in the US. Surveys of business confidence are hitting record lows. In the UK, the IHS Markit/CIPS services PMI score was 13.4 as at the end of the month (a figure below 50 indicates recession.) The previous record low was 40.1 in November 2008 during the global financial crisis. Similar lows were reached in the EU as the PMI indicator hit 13.5, and the US survey score was only 27.4.

Central banks stepped in very quickly using all the monetary tools at their disposal providing massive amounts of support to companies of all sizes to ensure the smooth functioning of markets and to retain the confidence in the financial system. The lessons from the Global Financial Crisis of 2008 have been learned and rewritten on an even bigger canvas. 'Unlimited buying' of government and corporate bonds, mortgage backed securities, and even higher yielding debt has staved off an unthinkable collapse in markets. The US Federal Reserve balance sheet has risen to $6.6 trillion, up from $4 trillion in February. Governments around the world drew up fiscal policies offering loans and grants to corporations, funding schemes to banks, and furlough schemes to protect businesses hit by the force of the shock.

April has seen global equity markets rally somewhat because of the size of the policy response. The MSCI World Index rose 9.1% in sterling terms, the US rose 11.2%, Europe was up 4.6%, UK up 3.4%, Japan 3.6% and Asia up 7.1%. Fixed income markets also enjoyed significant gains. However, we are likely to see weak economic data in the second quarter of this year to be released in July which will reflect further pressure on businesses who are struggling to stay afloat. Governments and central banks may have to provide even further emergency measures such as loans and grants to support the economy so that it can eventually re-emerge after the crisis has fully passed.

In a month of extraordinary events, one of the most unusual examples of the havoc reaped on the economy was the sudden fall in the oil price as we approached the month end for the May contracts. Due to the sudden collapse in demand for oil by industry and the transport sectors such as airlines, cars, trucks and cruise liners, coupled with the lack of storage facilities, sellers sought to offload their contracts and were paying buyers to avoid having to accept these 'unwanted' supplies. The price fell to minus $39 per barrel in the US. The June contract is currently priced at around $22, but still well below the average of $50.

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We had made changes to the model portfolios on three occasions before we entered April and rebalanced clients linked to those models to add more stability to the portfolios with the selling of riskier assets and the reallocation to cash and government bonds. Since the lows of 23rd March, the global equity markets have rebounded somewhat making up around half the difference, which may have led to opportunities for short-term traders, but we believe now is not the time to be taking unnecessary risks and so we intend to keep cash levels relatively high until we are confident that the global economy is emerging in better shape.

These are truly historic times and we must not lose focus of the fact that this is a health crisis before anything else which needs to be managed. We need to navigate the immediate icebergs, but we also need to look beyond the near-term issues and be well-positioned for the eventual resurgence of the global economy. There are some areas which have been obvious winners such as healthcare and pharmaceuticals but there are also those companies which have enabled us to videoconference with family, friends, and business colleagues. The rapid growth of online technology has enabled us to order our shopping, stream TV boxsets and films, play video games, as well as provide home schooling for our children. As one fund manager put it, we need to identify the ‘survivors’ and the ‘thrivers’ in the new world and avoid those companies who will fade and die.

The investment team continue to attend an extensive range of video meetings, telephone calls and webinars with fund houses, monitoring the funds in the model portfolios to remain on top of any changes to the portfolios themselves, whilst keeping a keen eye out for new strategies that will thrive in the future.

Andrew Graham - On behalf of the Investment Committee

NOTE: This material has been written for information purposes only and must not be considered as financial advice. Data as at 30th April 2020.