# Coronavirus Update

5th June 2020

It seems that the social distancing measures and the shielding of the vulnerable are working. The worst of the infection in Europe and the US at least is behind us as the rate of new cases has dropped off significantly, but the centre of the pandemic has shifted to Mexico, Brazil and Russia. The government is easing the lockdown measures gradually to prevent any new escalation in the infection rate whilst the risk of a second wave remains. In the UK, primary schools have started for certain year groups and there are social distancing guidelines for businesses waiting to reopen their doors.

Some European countries that have already started to ease their lockdowns are even planning to reopen tourist locations in such places as Spain, Greece, and Portugal. Italy declared 'coronavirus no longer clinically exists here' and has allowed all domestic travel to restart between regions. Airlines are planning on restarting services again in July and many countries with low infection rates are negotiating 'air bridges' to allow foreign travellers again. There may yet be an opportunity for a summer vacation abroad after all.

The economic data that came through towards the month end continues to confirm the heavy impact on the economy. Retail sales were down 50% in April. House prices were down 1.7% in May which is the largest fall in 11 years. Unemployment has risen sharply to over 2.3 million, with 8.4 million workers on furlough. The government announced that it would be extending the scheme until October although expects businesses to make a higher level of contribution. Over £21 billion in bounce back loans have been made. The Bank of England issued a three-year bond at a negative interest rate of -0.003% for the first time ever. In the US there are now almost 40 million unemployed, which is 15% of the workforce and is heading towards the levels seen in the 1930s. However, surveys of business confidence are rebounding after hitting historic lows in April. In the UK, the IHS Markit/CIPS services PMI score which was 13.4 as at the end of April is now at 29 (although a figure below 50 indicates recession.) In the EU, the PMI indicator hit 13.5 last month but is now up to 36, and the US composite survey score has risen to 37.

Central banks continue to provide massive amounts of stimulus to support the smooth functioning of markets and to retain the confidence in the financial system. 'Unlimited buying' of government and corporate bonds, mortgage backed securities, and even higher yielding debt has provided an essential backstop to global markets. The US Federal Reserve balance sheet has risen to over $7 trillion, up from $4 trillion in February. The EU has agreed a new €600 billion stimulus package of loans. The German government has separately provided a €9 billion bailout of Lufthansa and taken a 20% stake in the company. Japan also announced a new $1.1 trillion package as it became apparent it fell into recession following two quarters of negative growth at the end of 2019 and in the first quarter of 2020. Australia is also facing its first recession in thirty years. Its Reserve Bank has cut interest rates to a record low of 0.25%, launched its own unlimited bond buying programme and is facing its toughest conditions since the Great Depression of the 1930s.

We are likely to see weak economic data in the second quarter of this year which will be released in July and will maintain pressure on businesses who are struggling to stay afloat. Governments and central banks may have to extend even further emergency measures to continue to support the economy so that it can survive until the worst of the crisis has fully passed. Federal Reserve chair Jerome Powell warned of lasting damage and admitted that 'the recovery will come more slowly than we would like.'

May has seen global equity markets continue to rally, largely due to the ongoing support of central banks around the world as well as the view that the pandemic has stopped getting worse, especially in developed markets. The MSCI World Index rose 8.2% in sterling terms, the US rose 9.7%, Europe was up 6.6%, UK up 5.6%, Japan 10% and Asia up 5.3%. The S&P500 has now risen above 3000 for the first time since March and is approaching its pre-crisis highs. Fixed income markets have also enjoyed gains. Yields on government bonds from the major developed countries such


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as the US, Japan, Germany and the UK are at historic lows. In fact, the UK 2-year gilt traded with a negative yield for the first time. The extensive bond purchasing programmes of the central banks are intended to keep yields low and hence interest rates lower for longer to enable the economy to recover. This has also had positive effects in credit markets. Yields have come down as the risks of downgrades and defaults of large corporations on their debt obligations appears to have reduced. The oil price which experienced a spectacular fall to minus $39 per barrel in the US last month has rebounded strongly and the current price is around $40 per barrel. This reflects increasing demand for energy as economies reopen, the wheels of industry begin to move, and the population starts travelling again.

However, sadly we have witnessed some worrying political developments and social unrest. The death of George Floyd in Minneapolis last week sparked widespread rioting across the US and is reminiscent of scenes not seen since the riots of the 1960s. The National Guard was deployed to restore order in many states. Popular discord like this may well affect the gradual return to work and destabilise the recovery that many are anticipating. In China, the Communist Party passed a new national security law for Hong Kong that has been met with deep diplomatic concern because it undermines the principle of ‘one nation, two systems’ which was designed to ensure 50 years of democratic rights for Hong Kong following the handover in 1999. The US has said it may reconsider its special treatment of Hong Kong. The UK government has offered passports to 3 million inhabitants if the situation deteriorates. With trade tensions already high between China and the US, this situation may only accelerate the disruption to global supply chains as companies source production from countries other than China. Many companies may be forced to delist from the Hong Kong stock exchange and move to other friendlier locations, such as Singapore.

**Model Portfolios**

We had made two changes to the model portfolios during May by selling a global fund where the fund management team had departed, and we also sold a UK fund heavily exposed to sectors affected by the downturn. We have also rebalanced clients linked to those models which has had the effect of capturing gains made on riskier assets and reallocating to cash and government bonds. Although global equity markets continue to rally from the March lows, we are intending to keep cash levels relatively high as we are concerned that market valuations may now have become stretched, and until we are confident that the global economy is emerging successfully from the lockdown.

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

In another first, we conducted our own video conference for clients this month by Zoom. The presentation covered an update on the virus situation, the economic impact, as well as our outlook for this year. The session was recorded and is available if you missed it, so please contact your financial planner for more details. We intend to conduct further investment updates online in 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 31st May 2020.*