INVESTOR INSIGHT

Summer 2020 A look at the markets by RSMR

Welcome

Welcome to the latest edition of our 'Investor Insight' which provides high-level commentary on the global markets and how these might be affecting your investments.

We hope you find this useful.

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GRAYSIDE FINANCIAL SERVICES

The global economy: What's going on?

Investor hope as economic stimulus continues

As the world sinks into the deepest peacetime recession for 150 years, there remain glimmers of opportunity for investors. The last economic quarter was more positive than its predecessor but also more volatile, particularly in June with some localised coronavirus rises, especially in the US.

Although the pandemic still dominates international news, there has been some global stock market optimism and substantial gains from the March lows.

> "The last economic quarter was more positive than its predecessor but also more volatile."

There's better economic data from western economies and, significantly, China, as Purchasing Manager's Index (PMI) figures and manufacturing data rise from their deep plunge.

Technology and healthcare are benefitting from the crisis as reflected in company share prices and are sought-after by investors, which looks to be the case for some time. However, there are concerns for commercial property where retail and hotels are vulnerable and undergoing re-valuation.

As long as governments and central banks pump cash into national economies some stability is ensured but if there are further pandemic waves or negative vaccine news, investors will seek safe options where they exist.

The global economy remains fragile and markets will stay volatile for the next few months.

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The asset classes – a quick update

EQUITIES

As with previous crises, the initial reaction for risk assets was a significant sell off which could create investment opportunities for those able to move quickly.

This happened in March and markets have recovered strongly despite volatility from negative news. Global markets rose 17% on average, the strongest being the US, although Europe had a better June as the US flat lined.

Equities have been calmed by government and central bank intervention which has given investors the confidence to rebuild. Many economies face problems but markets have factored this in and are looking ahead.

While pandemic and economic news will continue to create volatility, 2021 and 2022 could be more positive as the global economy is likely to return to normal growth, especially if vaccines, or better treatments, become widely available.

There will still be huge stimulus in the financial system next year at a time of improving corporate earnings, so we should not feel too pessimistic about equity market prospects.

FIXED INTEREST

During the second quarter we saw relatively positive returns as some confidence appeared about improving economic conditions.

Government debt returns look meagre but many investors still hold them preferring safety due to the weak UK economy. Borrowing resulting from the financial support will not be fully financed by pension funds and insurance companies but by central banks through quantitative easing and other programmes.

Investors have been calling the end of the bond bubble for several years but it has still delivered surprising returns. It is not clear if this can continue and potential returns are likely to be lower.

Corporate debt still seems to offer the best opportunity but has greater associated risk than previously and is more closely linked to equities.

PROPERTY

There are still questions about commercial property as the market opens after accurate valuations have been restricted.

Landlords face acute problems in certain sectors, particularly with rents hit badly, especially in retail.

June saw all physical property funds continue to be suspended due to a lack of valuation evidence such as transactions, which affected trading and bank lending.

Retail and leisure rents are worst affected while industrials, warehousing and offices remain relatively strong. Lockdown is easing but restrictions and consumer trepidation prevent properties returning to pre-lockdown usage.

The UK government developed packages to alleviate some of these difficulties, including suspending business rates and providing bank loans, but debts must be repaid and this will hinder a profitable recovery.

There are some positives where transactions have picked up such as industrials and warehousing. Lockdown accelerated changes in office use and assessments may become more about quality than quantity with a rise in home working.

Lockdown also accelerated change in retail due to click and collect so, while properties will still be necessary, formats may change.

There are no easy solutions for property and many investors will have to remain locked out of these assets in the short term.

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Global round-up

- US spending bounced back in May, growing by a record 8.2% following a 12.6% drop in April.
- UK PMI data improved in June after the economy had its worst quarterly fall since 1979 of 2.2%.
- Covid-19 wreaked havoc on domestic and external demand in France, Italy and Spain.
- US unemployment data was unexpectedly positive in April adding 2.5m jobs.
- The EU economy is expected to contract by 7.0% in 2020.
- China's manufacturing has bounced back strongly helped by pent-up demand in global supply chains.
- In Mexico, preliminary data shows that the economy shrank for the fourth successive quarter.
- Japan's government issued stimulus worth roughly 20% of GDP in April to help businesses and consumers.

"China's manufacturing has bounced back strongly helped by pent-up demand in global supply chains."

So, what's next?

Emerging economies have suffered worse in the pandemic due to inadequate healthcare, overcrowded cities and being unable to create a strong enough fiscal response to protect incomes.

Until the pandemic's infection rate slows significantly, prospects in these emerging markets, including Brazil, Mexico, India and Indonesia, remain poor compared to the developed world. North Asia remains best placed in this region.

Economic data suggests a rapid initial bounce back for economies that locked down. How long this will last, and whether this is the start of a V bounce-back or if it flat lines, remains to be seen.

Western consumers have been sheltered from the worst economic impacts of Covid-19 through wage subsidy or, in the US, increased unemployment benefits. The US ends these in July, while European governments will phase out support in the autumn. This is likely to create challenges for businesses that deal personally with consumers.

Markets are not factoring in any major problems or setbacks to the economy, although a second international wave of infections would cause concerns.

In the short term valuations remain quite expensive, but current bond yields suggest alternatives to equities are not attractive for many investors either.

The US Federal Reserve has sent a 'do-whatever-it-takes' message to the markets and the European Central Bank is considering buying non-investment grade debt bonds.

Medium term investors should remain committed to equity markets but expect heightened volatility.

So far this year, markets have again proved that it is better to buy when the price is right and the news is bad than when the news is good but the price is high.

About RSMR

Independent specialist research.

RSMR was formed in 2004 to meet a growing demand from financial advisers for specialist and impartial investment research.

The RSMR team is made up of individuals with expertise from across all areas of the financial industry – from asset management, strategy and fund research through to business development, strategic planning and market research.

We are best known within the financial industry for our 'R' fund ratings – this rating is given to investment funds that meet our stringent research criteria. We don't limit ourselves to just looking at performance – we also look carefully at the people, processes and capabilities that are required to make effective investment decisions.

We work in partnership with your financial adviser, providing the benefit of our broad industry insight and rigorous research. This quarterly market summary is designed as a 'snapshot' of the more thorough and lengthy commentary that we provide to your adviser on a quarterly basis.

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