Stanhope Capital Fortnightly Bulletin

Period ending 31st March 2020

Tactical Positioning

The world is desperately trying to stop the spread of COVID-19 and heal the wounds caused by the virus. However, looking past the current news, at the infection cycle in China, South Korea and now Europe, it could be that we will be through the peak of the virus within 2 to 3 months. Although the US is lagging other countries, it may end up following a similar pattern to those hardest hit by the pandemic. The reaction by authorities, at a monetary and fiscal level, is huge, dwarfing the stimulus packages designed to support the economy during the Global Financial Crisis in 2008/2009.

Whilst market falls have been extreme, they recovered part of the fall towards the end of March. Our sense is that by the end of the third quarter of this year many people are likely to have returned to work and this should lead to some stabilisation in the global economy.

Turning to positioning, we have reduced our High Yield bond exposure in favour of adding to gold and/or equities. In the near term, depressed sectors such as energy, financials and leisure may bounce but we will continue to pursue our bias towards companies with 'quality growth' characteristics, namely those with strong balance sheets and sustainable earning growth. Alongside these we are also looking at infrastructure exposure as this should receive a substantial boost as governments look to breathe life into their economies.

Market Moves

	Equities (incl. Dividends)						
31-Mar-20	World ($)	US ($)	Europe[1] (€)	UK (£)	Japan (¥)	EM ($)	Asia ($)
From March 16th	-1.4%	-4.6%	7.9%	5.9%	11.0%	-3.1%	-3.9%
Month to Date	-12.8%	-12.4%	-13.7%	-13.4%	-7.1%	-13.0%	-12.8%
Year to Date	-20.0%	-19.7%	-21.1%	-23.8%	-17.3%	-19.1%	-17.5%

	Commodities			Currencies (vs. USD)			Gov't
	COM[2] ($)	Gold ($)	WTI Oil ($)	EUR	GBP	JPY	UST 10Y[3]
From March 16th	-5.3%	3.1%	-35.5%	-0.7%	1.2%	0.3%	-29bps
Month to Date	-12.8%	-0.5%	-54.2%	0.0%	-3.1%	0.5%	-48bps
Year to Date	-23.3%	3.9%	-66.5%	-1.6%	-6.3%	1.0%	-125bps

Note: [1]Europe excluding UK; [2]Bloomberg Commodity Index; [3]US Treasury 10 Year Yield shows absolute, not percentage, change in yield; Source: Bloomberg

The second half of the month continued as it started with investors spooked by the uncertainties and growing economic impact of the coronavirus and the lockdowns being enforced across many countries. On 16th March, global equity markets endured yet another day of punishing falls with the Dow Jones Index falling 12.93%, the worst daily drop since 1987. This set the tone for much of the following week. The speed and scale of the rout in equity markets combined with extreme volatility spikes led to widespread selling across bond, commodity and currency markets, as leveraged investors liquidated assets indiscriminately to meet immediate margin call requirements. Haven assets, which traditionally perform well in market falls, such as gold, the Japanese yen and US Treasuries also fell during various stages of the sell-off.

The US dollar became the world's most desired paper (after loo roll) as market participants bought it, either as a safe haven asset or to meet future costs. This led the dollar to have its biggest rally for five years and caused sterling to tumble to a 35-year low of $1.14 from $1.31 at the beginning of March.

The last week of the month saw stocks rebound as investors appeared encouraged by further aggressive monetary policy actions and unprecedented firing of fiscal bazookas. On 24th March, the Dow Jones Index had its best day since 1933 and the S&P 500 Index experienced its largest daily rally since October 2008, as many developed equity markets surged around 10%. By the close of business on 26th March, the Dow Jones Index marked its best three-day stretch since 1931. Despite this, major indices subsequently surrendered a small portion of these gains as the month ended, owing to further negative news of the virus's spread

The rebound from the market lows witnessed in the last week of March could be a sign that markets have already priced in the worst of the economic fallout, before we have even hit the peak of this health crisis. Whether this is the case is impossible to predict, as we still do not know how bad the impact of the pandemic will be. What we do know is that events have forced the hand of governments and Central Banks across the world to implement enormous monetary and fiscal measures in an attempt to keep their economies afloat.

The US House of Representatives finally approved a $2.2 trillion stimulus package, including $350 billion in support of small businesses, along with $1,200 direct payments to lower and middle-income adults. The US Federal Reserve (the 'Fed') pledged that it was setting no limit on its purchases of Treasuries and Agency mortgage-backed securities. The Fed also announced that it would buy corporate bonds and for the first time in history, include the riskiest investment grade debt.

The European Central Bank ('ECB') fell short of another 'whatever it takes' moment when it announced a €750bn emergency bond purchase scheme with its newly titled Pandemic Emergency Purchase Programme ('PEPP'). The scheme, set to last until the ECB judges that the Covid-19 crisis is over, will see the it buy government bonds, private sectors bonds, and for the first time, non-financial commercial paper. This can hopefully provide a powerful backstop for the European corporate credit space.

Economic Updates

Data releases during the fortnight were largely ignored as the true impact of the coronavirus will start to filter through in April, when the March readings are published. However, initial jobless statistics in the US revealed a staggering 3.3 million new unemployment claims, up from the prior week's reading of 282,000. For context, we have never seen a reading above 700,000 before. Surprisingly the stock market rose sharply on the day of this announcement with the S&P 500 posting gains of nearly 6.3% - possibly a sign that much of the bad news is already reflected in current prices.

There was some positive news as China's Purchasing Managers' Index ('PMI') readings beat market expectations, bouncing into expansionary territory, largely driven by a sharp rebound in production, employment and orders. According to state media reports, the manufacturing PMI jumped to 52.0 for March. This was higher than the 44.8 analysts expected, and up from 35.7 in February, which was the worst month since China began recording the data in 2005. Meanwhile, the services PMI came in at 52.3 versus the 42.0 expected and 29.6 surveyed in February. China may provide a guide as to how quickly economies can recover, but as China begins to roll back its lockdown restrictions, all eyes will surely be focused on whether a second wave of the coronavirus stalls its progress.

JONATHAN BELL
IVO COULSON
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2nd April 2020

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