Stanhope Capital

Stanhope Capital Fortnightly Bulletin

Period ending 15th April 2020

Tactical Positioning

The last fortnight is a good reminder that getting too bearish risks missing out when markets rise. As we discuss below, the S&P 500 index has just had one of its best ever weeks. Trying to time markets is proving (as always) to be hazardous and whilst emergence from COVID-19 may not be a ‘V’ shaped experience for global economies, stock markets look at things differently and a ‘V’ shaped recovery for equities (at least partially) should not be ruled out. Although a flattening out in infections and an easing of lockdowns lifts investor sentiment, it is the colossal fiscal and monetary packages that are lifting the price of risk assets.

We remain close to full weightings in equities and, whilst accepting that there are still significant risks, we have no plans to alter the magnitude of our exposure at the current time, although we may slightly adjust our positioning. Looking ahead, we anticipate that bonds will only have a minor part to play in portfolios and that gold will remain an important element. Quality growth companies, technology and healthcare seem to be lasting themes and we will continue to have high exposure to them in our equity budget.

Market Moves

	Equities *(incl. Dividends)*						
15-Apr-20	**World ($)**	**US ($)**	**Europe[1] (€)**	**UK (£)**	**Japan (¥)**	**EM ($)**	**Asia ($)**
Month to Date	5.6%	7.8%	1.0%	-1.6%	2.8%	4.8%	5.0%
Year to Date	-15.5%	-13.5%	-20.3%	-25.1%	-15.0%	-15.2%	-13.4%
	Commodities			**Currencies (vs. USD)**			**Gov't**
	COM[2] ($)	**Gold ($)**	**WTI Oil ($)**	**EUR**	**GBP**	**JPY**	**UST 10Y[3]**
Month to Date	0.2%	8.9%	-3.0%	-1.1%	0.8%	0.1%	-4bps
Year to Date	-23.2%	13.2%	-67.5%	-2.7%	-5.6%	1.1%	-129bps

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

With the exception of the UK, equity markets rallied over the first two weeks of the month, in response to the flattening of new coronavirus cases and fatality rates around the world, as well as the first steps towards the loosening of social distancing restrictions in Europe. Wall Street entered a technical bull market, rising 7.8% over the fortnight and up over 20% since its low on March 23rd, with its correlation to the changing rate of new coronavirus cases in Italy remaining high. Putting this rally into context, the S&P 500 index experienced its eighth best week ever, out of the 4,184 weeks since records began. Those companies well placed to benefit from the closure of shops and people being forced to stay at home, such as Amazon and Netflix, were amongst the standout performers.

By 15th April, there were more than two million reported COVID-19 cases and more than 125,000 known related deaths. This represented a doubling of new cases over 13 days, whereas previously it had taken eight days for the number of cases to double. Markets appear to be pricing in a V-shaped economic recovery. In practice, governments are likely to face challenges to successfully implementing rapid exit strategies from the various forms of “lockdown” and the economic impact of the pandemic might be more protracted. Looking forward, with the corporate earnings season underway, investors’ confidence is perhaps set to be tested again.

Central banks continued their unprecedented efforts to support coronavirus ravaged economies. In the US, the Federal Reserve (“FED”) declared a $2.3 trillion package designed to support small businesses and municipalities, including measures to buy Investment Grade and High Yield bonds. Despite the plan to purchase High Yield being relatively small, it is crucially the first time a major central bank has purchased non-investment grade bonds and importantly clears the path for further exploits into the high yield space. The FED's willingness to intervene prompted spreads on US High Yield and Investment Grade bonds to tighten sharply over US Treasuries. This side of the Atlantic, the UK, pushed towards the direct financing of government spending by its central bank, as the Bank of England temporarily agreed to cover the cost of some emergency policies, including the Coronavirus Job Retention Scheme.

On the continent, the Eurogroup (a meeting involving the finance ministers of member states in the European Union with the euro as their currency), took centre stage. While ministers agreed a €500 billion emergency rescue package supporting businesses and workers, their failure to agree on how to pay for the longer-term recovery plan to deal with the crisis, weighed on markets. Tensions between Northern and Southern member states concentrated on Italy's refusal to accept certain conditions attached to the European Stability Mechanism's credit line. Any progress in this dispute could rest on the attractiveness of the EU's recovery fund to Italy, the details of which should be made public later this month.

Alarming forecasts announced by the International Monetary Fund ("IMF") at end of the fortnight stoked concerns about a slump in demand for oil. In its latest World Economic Outlook report, the IMF forecast that global GDP would contract by 3.0% over 2020, easily surpassing the 0.1% decline during the Global Financial Crisis in 2009. The organisation also revealed that it expected aggregate Developed Economy GDP to decline by 6.1% and Emerging Economy GDP to fall by 1.0%. Prior to this, oil prices had climbed as Russia and OPEC heavy weight, Saudi Arabia, finally agreed to end their price war and committed to cutting production by 9.7 million barrels per day. Yet, oil prices ended the period down 3.0%, with the impact of the production cut neutered by fears about substantial declines in demand for oil, alongside fresh concerns about oversupply, owing to the publication of a report by the American Petroleum Institute, showing US crude inventories having surged by 12.1 million barrels in a week.

Economic Update

Economic data released over the fortnight was extremely poor. "Lockdown" measures in the US had a suffocating effect on its economy. Industrial production fell by 5.4% over March, its largest monthly decline since the end of the Second World War, whilst retail sales fell by 8.7%, the worst fall since records began in 1992. In the fine print, clothing sales were down by 50.5%, and furniture sales dropped by 26.8%. A sharp rise in unemployment, the scale of which took almost all economists by surprise, severely dented consumer confidence. Weekly jobless claims spiked to 6.6 million, double the previous reading of 3.3 million and considerably higher than at the peak of the Global Financial Crisis in March 2009, when 665,000 weekly jobless claims were recorded. (The situation was compounded by a further 5.2 million first time jobless claims being filed on 16th April).

Europe also experienced a deterioration in economic data posted over the period. The IHS Markit Eurozone Composite Purchasing Manufacturers Index ("PMI") was revised down to an all-time low of 29.7, far beneath the 51.6 recorded in February (above 50 suggests an expansion in manufacturing). In France, the government ominously warned that its economy would shrink by 8% in 2020 and that the budget deficit would rise to 9% of GDP. The picture was similar in the UK, where the UK's Office of Budget Responsibility forecast that the economy would contract by 35% over the second quarter and borrowing would rise to 14% of GDP in 2020/21. Elsewhere, new car registrations in March fell by 44.4% year-on-year. Prime Minister Johnson's admittance to intensive care with coronavirus threatened turning a health and economic crisis into a constitutional crisis. Fortunately, he subsequently recovered and our spirits were lifted by Captain Thomas Moore (age 99, garden laps completed 100) who stated that "*For all those people who are finding it difficult at the moment: the sun will shine on you again and the clouds will go away*".

JONATHAN BELL
IVO COULSON
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15 April 2020

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