Stanhope Capital Fortnightly Bulletin

Period ending 31st May 2020

Tactical Positioning

As we discuss below, equity markets have been strong over the past few weeks and our portfolios continue to benefit from the recovery. However, looking into the second half of 2020, one source of increasing concern is the performance of sterling against a background of difficult Brexit trade negotiations, significant money printing and interest rates that may head into negative territory (not to mention a huge, looming budget deficit). Although the pound looks reasonably cheap on a 'purchasing power parity' basis, it is a small and volatile currency which tends to perform badly when risk assets are in retreat. Taking all these factors into account, we have reduced our sterling exposure for clients who have it as their base currency. It is worth noting that during the market stress of late March, the pound fell to $1.15 versus the dollar but has subsequently recovered to around $1.25. We believe that there is scope for sterling to revisit these lows in the coming months.

Market Moves

	Equities *(incl. Dividends)*						
31-May-20	**World ($)**	**US ($)**	**Europe[1] (€)**	**UK (£)**	**Japan (¥)**	**EM ($)**	**Asia ($)**
Last 2 Weeks	6.0%	6.4%	7.6%	4.9%	7.7%	2.5%	1.7%
May	4.2%	4.7%	4.1%	3.3%	6.7%	0.6%	-0.2%
Year to Date	-8.0%	-5.2%	-12.8%	-18.2%	-7.9%	-11.4%	-10.8%

	Commodities			Currencies (vs. USD)			Gov't
	COM[2] ($)	**Gold ($)**	**WTI Oil ($)**	**EUR**	**GBP**	**JPY**	**UST 10Y[3]**
Last 2 Weeks	3.0%	-0.9%	20.6%	2.6%	1.9%	-0.7%	1bps
May	4.3%	2.7%	88.4%	1.3%	-2.0%	-0.6%	1bps
Year to Date	-21.2%	13.8%	-41.9%	-1.0%	-6.9%	0.8%	-126bps

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

Equities ended the fortnight higher driven by additional central bank announcements, government support and hopes of a continued economic recovery as countries emerge from lockdowns. Europe and Japan were the standout performers, with the US close behind. During May as a whole, the US technology sector continued to lead the way, with the NASDAQ index now up an impressive 4.9% this year. It will be interesting to see whether it can keep up its momentum as shares in Facebook and Twitter come under pressure from President Donald Trump's threats to tighten regulations on social media platforms following Twitter's posting of a fact-check notice regarding one of his tweets.

Gold fell slightly during the fortnight and even though the price of WTI Oil saw a staggering 88% gain over the course of May, it is still down 41.9% in 2020 so far, reflecting just how savage the demand drop and oversupply have been. Bond yields in the US were flat, whereas European periphery country bond yields fell following the European Commission's announcement of a planned recovery fund (more below).

The past two weeks also saw a slew of negative developments and mounting tensions. The US Senate adopted a draft bill enabling increased surveillance of non-US companies, which in the worst-case scenario would exclude Chinese companies from US listings. Riots and looting have been plaguing many cities across the US since the death of George Floyd. What initially started out as peaceful protests by the "Black Lives Matter" movement, has escalated with the involvement of Antifa (the anti-fascist protest movement) and its supporters. In response President Trump has declared that Antifa will become a designated terrorist organisation, however it is unclear what implications this will have.

Thursday’s jobless claims report showed that an additional 2.4 million Americans filed for unemployment in the previous week, bringing the trailing nine-week total to a stunning 39 million. While many economists believe that it is possible for millions of displaced workers to be rehired in the summer months as the economy slowly reopens, they warn that many other expected temporary layoffs could turn into permanent job losses, specifically across the retail and hospitality sectors.

In Europe, Germany and France proposed a €750 billion European Union recovery fund, in order to coordinate a European fiscal response to the coronavirus pandemic. The European Commission is planning to raise the money in the capital markets and use €500 billion to support EU spending in the form of grants and €250 billion in loans to national governments. “The Frugal Four”; Austria, the Netherlands, Denmark, and Sweden oppose the plan, saying they would only accept a rescue fund that exclusively gives out loans rather than grants. If European Commission President Ursula von der Leyen can win the backing of member states, it would be a watershed moment for the bloc, where financial burden sharing has long been one of the thorniest issues that has held back deeper integration. It could quell concerns that a lack of solidarity is empowering populists and in turn threatening the EU’s survival. Italy and Spain would be the biggest beneficiaries of the rescue package, with their economies having been hit hardest during the pandemic.

In the UK, Bank of England Governor, Andrew Bailey, made a U-turn on his previous comments regarding negative interest rates, by telling a parliamentary committee that negative interest rates were now under “active review” to reinforce an economic recovery. He made it clear that policymakers would need additional time to consider the implications of such a move. The week before he said that the central bank was neither planning nor contemplating negative rates, although he declined to rule them out altogether.

Economic Updates

Economic reports released during the fortnight looked encouraging. In the US, the IHS Markit’s gauge of May services sector activity surprised on the upside, existing home sales in April were also modestly stronger than expected and mortgage applications jumped in May off a five-year low.

China’s National People’s Congress re-opened in Beijing and for the first time since 1994 there was no official growth target set, giving policymakers more flexibility in reopening the economy, without the need to worry about meeting, what Chinese premier Li Keqiang called, a "man-made" target.

We are starting to see the first high-profile bankruptcies (such as Hertz Rental Cars) and multiple government bailouts for severely damaged key-industry players. For example, Lufthansa, the German air carrier, has been losing an average of €1 million an hour since the pandemic started and is set to receive a €9bn bailout from the German government in exchange for a 20% stake, two board seats and a veto over any hostile takeover bid. Germany said it is planning to sell its shares by the end of 2023.

JONATHAN BELL
IVO COULSON
STEFAN KUTZNER
31 May 2020

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