Stanhope Capital Fortnightly Bulletin

Period ending 31 July 2020

Tactical Positioning

July saw major moves in currencies and commodities, whilst growth-focussed equities continued to outperform other areas of the market. August is historically a difficult month for investors thanks to lower trading volumes and a lack of guidance from holidaying central bankers. This year, with COVID-19 and the oncoming US presidential election, some investors might be tempted to take a more cautious stance, especially given the sharp V-shaped recovery in many equity markets set against a shallower economic rebound. Notwithstanding, we remain largely invested in equities as a significant amount of liquidity remains available for investment. This money tends to seep into risk assets over time and this seems likely whilst 'safe-haven' investments offer little or negative yields.

Market Moves

	Equities *(incl. Dividends)*						
31-Jul-20	World ($)	US ($)	Europe[1] (€)	UK (£)	Japan (¥)	EM ($)	Asia ($)
Last 2 Weeks	-0.4%	1.4%	-4.7%	-6.2%	-5.7%	1.1%	0.2%
July	4.0%	5.6%	-0.5%	-4.2%	-3.6%	8.1%	6.9%
Year to Date	-1.6%	2.0%	-10.0%	-20.4%	-11.1%	2.2%	1.7%

	Commodities			Currencies (vs. USD)			Gov't
	COM[2] ($)	Gold ($)	WTI Oil ($)	EUR	GBP	JPY	UST 10Y[3]
Last 2 Weeks	3.0%	9.1%	-2.3%	3.2%	4.0%	1.0%	-10bps
July	5.7%	10.9%	2.5%	4.8%	5.5%	2.0%	-13bps
Year to Date	-14.8%	30.2%	-34.0%	5.0%	-1.3%	2.6%	-139bps

[1] *Europe excluding UK*

[2] *Bloomberg Commodity Index*

[3] *US Treasury 10 Year Yield shows absolute, not percentage, change in yield*

Source: Bloomberg

The fortnight was a microcosm of the market trends and economic upheaval we have seen so far this year. For lockdown beneficiaries, it was a stunning fortnight, with results from the leading US technology names beating earnings expectations whilst the Congressional anti-trust hearing involving the CEOs of Apple, Alphabet (Google), Facebook and Amazon barely impacted bullish sentiment. COVID-19 and the resultant restrictions have hastened the move to a digital economy, meanwhile the US Federal Reserve (Fed) has delivered a sharp fall in the cost of capital through lower long-term interest rates which particularly help growth stocks. The NASDAQ composite index delivered a 6.9% return in July, taking it to up 20.5% year-to-date.

Meanwhile the US dollar had its worst month in a decade, losing 4.2% against a basket of six other currencies, partly owing to concerns that the increase in the money supply will ultimately devalue the currency. By contrast, precious metals benefitted from concerns relating to the devaluation of money and, on a more short-term basis, from inflows by retail investors and systematic traders. Gold rose 10.9% over the month and the metal is now up over 30% this year in US dollar terms. Silver, playing catch-up with gold, had its best month in 40 years, returning 34.0% in July.

Elsewhere, other equity indices performed poorly in local currency, although they performed similarly to US equities in dollar terms, given the fall in the dollar. The more cyclically exposed European and Japanese indices were lower on fears of a resurgence of the virus and a further economic slowdown. This is despite the announcement of the €750 billion EU recovery fund made up of grants and loans to member states. European banks are down 37.5% this year (-5.4% in July), reflecting concerns about loan losses, the economic outlook and the path of monetary policy.

In the bond markets, US Treasury prices rose, and the benchmark US 10-year yield hit a record closing low of 0.528%. In the corporate bond market, credit spreads (the additional yield over government bonds) broadly tightened during the fortnight on the back of increased purchasing by yield-hungry investors. US high yield (lower quality) bonds were the standout performer with the credit spread over government bonds tightening by 0.58%.

The combination of higher prices for precious metals, bonds and equities in the US could be the result of quantitative easing which is pushing up the price of financial assets. Unlike the period after the global financial crisis, US money supply has increased by over 20% since the start of the year and we remain concerned that the long-term impact of central bank policy could be inflationary, so we continue to favour real assets that offer some inflation protection.

On 31 July, funding for additional US unemployment benefits worth $600 per week under the CARES Act ended as Congress was unable to agree an extension or replacement. Republicans want to cut this to $200 per week to encourage people back to work as the benefits package led to some Americans having more income after being laid off than when they were working. Meanwhile, Joe Biden's lead in the polls over President Trump may be the reason that the President called for a postponement of the November presidential election, citing alleged postal voting fraud. It is highly unlikely that the election will be postponed as it would require a constitutional amendment to do so. In any event, the election is likely to be dominated, if not determined, by the progress and management of COVID-19.

On monetary policy, the Fed announced on Wednesday that "Following sharp declines, economic activity and employment have picked up somewhat in recent months but remain well below their levels at the beginning of the year". As a result, interest rates were left unchanged and there were no new policy announcements.

Economic Updates

Second Quarter Gross Domestic Product data for the US and Eurozone revealed a 32.9% quarter-on-quarter drop in the US and a 12.1% drop in the Eurozone.

The latest Purchasing Managers' Indices (PMIs) showed a divergence in recovery in the US and Europe; for the Eurozone the indices came in at 55.1 (services) and 51.1 (manufacturing) – a figure over 50 indicates expansion. However, in the US, the same came in at 49.6 and 51.3 respectively – indicating the service sector is still in contraction, although the figure is an improvement on 47.9 seen last month.

JONATHAN BELL
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31 July 2020

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