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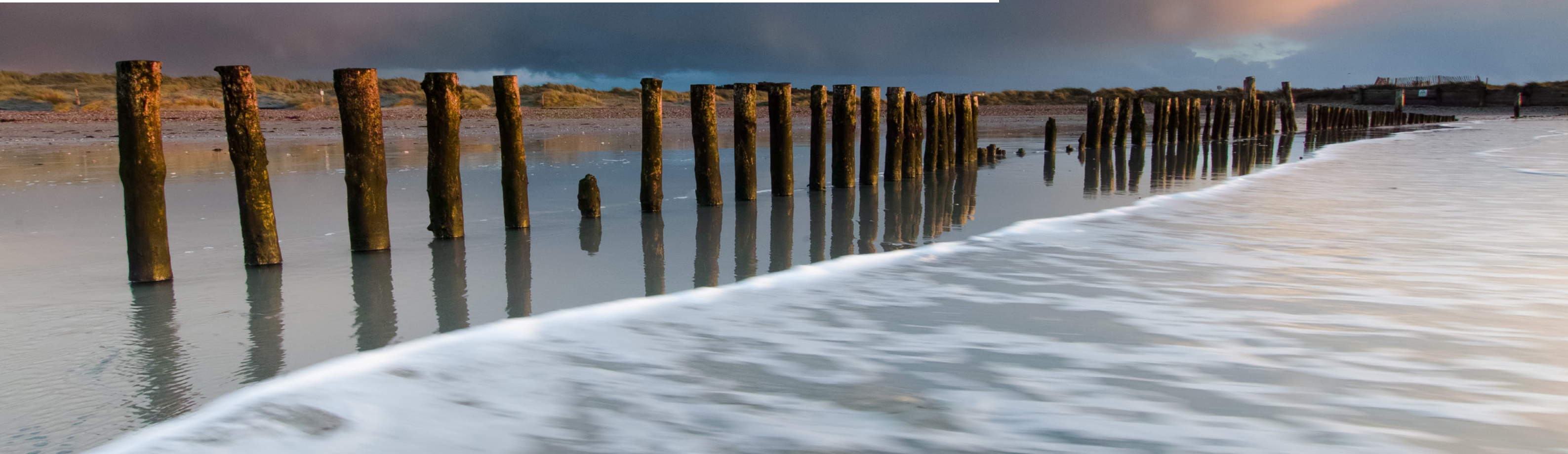
Asset Management

State of play



08 April 2020

In the midst of this unprecedented global event, our Investment Specialist, Simon Durling, provides you with the latest COVID-19 developments, alongside our market and investment insights.

As the respective "lockdowns" across the world continue governments are faced with vitally important decisions about what comes next in the fight against this invisible enemy.

Juggling restrictions of movement, civil liberties and economic consequences is a very fine balancing act, not least when set against a backdrop of differing expert scientific and medical opinions on which exit strategy is the best to implement.

All of these decisions are being tested against the court of public opinion as restlessness and heated exchanges on social media highlight the public's craving for answers as to the how's and when's of a return to normal life.

Economic impacts and response measure

Ever since the COVID-19 outbreak, there has been a lot of evaluation of the economic impacts of pressing the pause button on the global economy. To date various governments have stepped in with unprecedented financial measures to help cushion the blow, but as yet it is impossible to truly tell until much later whether these will work.

The biggest impact of shutting down an economy has been on peoples jobs. In the US, following a record number of unemployment claims the previous week, the latest figures provided chilling reading, with more than 6.6 million individual claims, bringing the two week total to just shy of 10 million in just 14 days. That has pushed up the US unemployment rate from 3.5% prior to the crisis to 4.4% in just one month.[1]

[1] Investing.com

Whilst the financial interventions have been record breaking, even the $2.2 tn package in the US is seen by many as inadequate. Speculation has spread that an additional $1.2 tn may follow in due course. Many experts argue that this is unchartered territory, explaining that in certain sectors, even if a business has access to financial liquidity or loans to keep the doors just about open, it does not help them replace lost business. In simple terms, if you and your family have a favourite restaurant and tend to visit twice a month, during a potential lockdown of three months, that is six meals at perhaps £60-100 each time. After the crisis passes, that restaurant will not recover the £600 you may have happily spent in those visits. A loan may avoid closure for now, but it cannot recover lost revenue for some businesses, especially in the services sector.

Over the last two decades there has been a drive towards globalisation which has arguably kept inflation below the long-term average. However there have been signs more recently that this is declining. This has been influenced in part by the US-China "trade war", but also by other factors. Rising costs in emerging markets and advances in technology have made onshoring your manufacturing much more attractive. What this pandemic has highlighted is the fragility of the "just in time" supply chains that form the basis of our modern global economy as industry after industry has shutdown. It is reasonable to accept that companies may now localise supply chains and prioritise durability over cost to reduce future vulnerabilities. This has the potential to reverse the inflation benefits.

So far the global economy has experienced an acute demand shock, where nobody is buying anything, or very little of it, except for basic necessities. Within a short period of time, we are likely to face a supply shock, because businesses are shutting down, or working at much-reduced levels. Once the lockdowns are over, there is likely to be a strong wave of pent-up demand for goods, goods which may have had their supply chain impacted, leaving a very limited supply available. With governments taking massive measures to sustain aggregate demand in a shutdown world, it is fair to assume that more money will be chasing fewer goods, which could result in higher inflation in the coming months.

Market conditions

Stock markets in the last couple of days have taken heart from encouraging signs that the pandemic rates are flattening in certain countries and increased policy measures to tackle the economic fall out. On 6 and 7 April, various stock markets rose 4-6% in just two days.

However, volatility remains, with investors expecting more bad economic news to come and keeping in mind that whilst infection rates appear to be slowing, how the world exits lockdowns and gradually manages their economies back to normal is fraught with danger. As I have said in previous blogs, this is unchartered territory and nobody can be sure what the long-term impacts of shutting an economy will be. Any positive news

on treatments, antidote tests and ultimately a successful vaccine test are likely to be greeted with investors returning to markets in droves, however, it appears that these developments are some way off. In the meantime, markets are very sensitive to bad news, especially if the expectations of recession prove to be worse than expected. The current "relief rally" could be very short indeed.

To add to the volatile landscape, a deal on the Oil Price War of the magnitude being discussed (10-15 million barrels per day), is possible but difficult. Much will depend on how much pressure the US is willing to put on Saudi Arabia and Russia as well as what production control measures the US is able to muster up domestically. The other option being floated is the use of tariffs to reduce US foreign oil imports and thus protect US shale, but there are serious questions over how effective this measure would be given the composition of US oil imports. With a meeting scheduled for later this week, a production cut is far from a done deal and investing in oil-related assets warrants additional caution.

Find out more

Read our latest **A Month in the Markets** by Portfolio Manager, John Mullins, for his full review of March and his outlook for markets as we continue to navigate the volatile climate during COVID-19 **here**.

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