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Santander Asset Management

State of play

4 June 2020

Our Investment Specialist Simon Durling shares his thoughts on the latest COVID-19 developments and the key stories impacting markets over the past week.

News this week

For the first time since I began writing a weekly blog in response to the COVID-19 outbreak on 26 March, the headlines have featured stories beyond the crisis. However, I will start with a quick round up of the latest on COVID-19 and then touch on some other key stories.

Latest on COVID-19

On 1 June some schools in England re-opened for the first time since lockdown, with Reception, Year 1 and Year 6 children returning. The attendance across the country was varied as some parents felt it was too soon to send their children back, while some Local Authorities have delayed their planned re-opening until 15 June concerned that the risks remain too high to safely re-open in their area. The infection and death rates announced this week are the lowest since March - a sign that the lockdown has helped to slow the virus - although many have mixed views as to whether the UK Government was too slow to enter lockdown and too early to lift restriction measures. The latest changes this week allowed people to gather in groups of up to 6, provided it is outside and at least 2 metres apart. Many have taken this as an opportunity to re-connect with loved ones after many weeks apart whilst thousands have taken advantage of the lovely weather targeting beaches and parks.

Unrest in US cities escalates

Many US cities were rocked by growing protests triggered by the killing of an unarmed black man by Minneapolis police. Two separate autopsies conducted on George Floyd came to the conclusion of homicide, but offered different causes. Whilst many protests were peaceful, outbreaks of looting and violence prompted warnings by President Trump that he would send in combat troops if state governors were unable to control the situation. The last few days have represented some of the worst civil unrest in the US for decades. The protests and the violence threatened to dent consumer confidence as the US economy is trying to reopen after lockdowns have been lifted. The latest developments are seen by some as a blow to President Trump's re-election plans given the criticism he has faced on the handling of the COVID-19 crisis and the economic damage that has been inflicted during lockdown. Whilst many would caution against writing off President Trump, the latest developments are starting to erupt into political fires that look potentially difficult to extinguish by November's election.

Markets cautiously back shorter trading day

Following a consultation, proposals to shorten the stock market trading day to just seven hours have been cautiously backed by market makers, investors and brokers. The London Stock Exchange said that there was broad agreement within the industry and among its customers to reduce the trading day, as long as it could be co-ordinated with other European exchanges. The changes have been suggested by some groups to reduce stress and boost diversity. They say that the change would boost liquidity as the same volume of orders would be conducted across fewer hours. It is also hoped to attract more working mothers into city careers. The consultation suggested moving from the current London opening hours of 8am until 4.30pm to a shorter time slot of 9am until 4pm. Most European exchanges open and close at exactly the same time regardless of local time differences. Euronext began its own consultation on 31 March, which has yet to be concluded. Others are also exploring shorter hours, with Deutsche Börse Group expressing doubts about the idea.

Economic news

Brexit fishing compromise may have repercussions

Talks continue this week between the UK Government and the European Union (EU) on fishing rights with hopes raised that a deal could be reached very soon. This may lead to one of the biggest obstacles to a future free trade agreement, as French fisherman would be prevented from catching a sizable proportion of their current weekly catch. Assuming a compromise is reached, the implications for other European countries and France, in particular, could lead to the potential for a blockade in the port of Calais (the port at Calais is very narrow making it easy for just a few vessels to block traffic). This threatens nearly one fifth of goods the UK trades - totalling more than £100bn. The UK Government is understood to have made plans to mitigate the effects of a blockade as part of its no-deal preparations last year, but it would still cause widespread disruption. Britain has presented proposals for annual fishing quotas with the EU based on “zonal attachment”, which reflects where fish live. The current system means European fishermen catch over six times more fish than British fishermen from the UK coastal waters. David Frost, the Prime Minister’s Chief Brexit Negotiator, and his team are to hold a fourth round of talks this week with the EU signalling it is ready to compromise on quotas. France has apparently privately warned other European governments that blockades would begin within 24 hours of any deal announcing cuts to catches. The EU and UK begin their last round of talks on trading relations after the current post-Brexit transitional phase lapses at the end of the year. The UK Government has said it won’t seek an extension of the transition period, which has kept conditions for businesses effectively unchanged since the UK formally left the bloc earlier this year.

US Government analysts paint a gloomy recovery picture

Government analysts have predicted the US economy will take almost a decade to recover from the pandemic. They expect the virus will cost $7.9tn by the end of 2030. The Congressional Budget Office, the non-partisan agency, adds to a growing body of research suggesting that there will be no “v-shaped” recovery for the US economy - whereby it bounces back to pre-pandemic measures within a year or so. The report issued said the recovery is expected to be “swoosh” shaped - where a small initial bounce is followed by a long, slow climb. Approximately 40 million people lost their jobs in the ten weeks after federal and state governments began lockdown. During April, data shows that manufacturing slumped whilst consumer spending collapsed, sectors which drive more than two thirds of the US economy. Phillip Swagel, Director of the Congressional Budget Office, said: “business closures and social distancing measures are expected to curtail consumer spending, while the recent drop in energy prices is projected to severely reduce US investment in the energy sector”. He said that previous fiscal stimulus by Washington, worth $3.3tn, would “partially mitigate the deterioration in economic conditions”. Real gross domestic product will be $724bn, or 13.3%, lower in the second quarter of this year than the Congressional Budget Office’s January forecast. The monthly jobs report on Friday is forecast to show that unemployment in the US rose to 20% last month from just above 3% before the crisis.

Market roundup

Following last week's update, stock markets around the world have hit new highs since the end of March lows that followed the lockdowns that paused the world's economy. Signs of economic recovery from the COVID-19 pandemic and additional stimulus has provided optimism for investors, helping to drive stocks higher despite the civil unrest in the US. The Nasdaq, heavily influenced by big technology stocks, is only 3% from its pre-pandemic highs. The latest Purchasing Managers Index data pointed to a fragile but encouraging bottoming in global manufacturing, raising hopes that the worst is over. The German stock market hit a three-month high, pulling European markets in its wake, amid reports that the German Government was going to debate a further stimulus package to the economy. The reports proved accurate and on 3 June a package worth €130bn was announced. Bond markets remain more cautious about whether the global economy is through the worst as the benchmark 10-year US Treasuries yields fell to 0.66% late on 1 June. The UK Government bond yields remain negative on short-term issues and the 10-year rate is still near all-time lows at just over 0.2%. The US dollar was at multi-month lows against most major currencies following a 5% drop caused by concerns about the rising civil unrest is many US cities. Hopes for rising demand from an economic rebound boosted oil prices. US Crude oil recently rose to $35.92 per barrel and Brent oil was at $38.70 as at 2 June.

Find out more

Listen to our latest **Market Views: Check point** update with John Mullins, Portfolio Manager, as he discusses how the team is positioning itself as we continue to navigate the volatile climate during COVID-19 **here**.

Note: Data as at 2 June 2020.