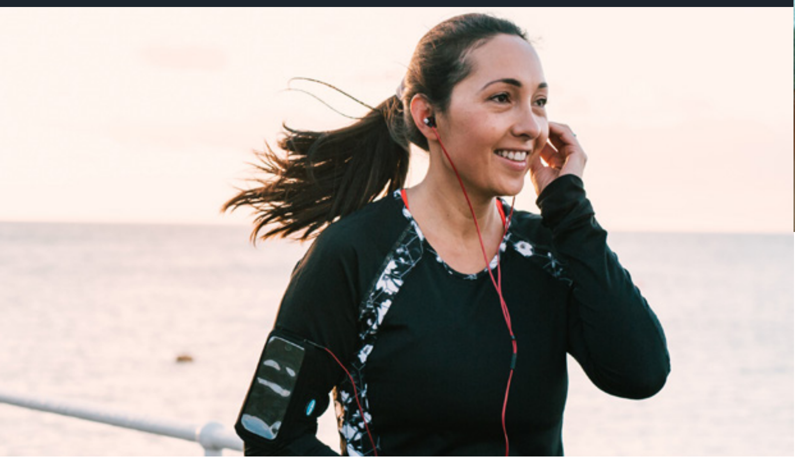
A month in the markets

By John Mullins

March 2020



John Mullins

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Month of February

Market Review

February saw an aggressive repricing of global stock markets as investors navigated uncertainty around the economic impact of the ongoing Coronavirus (COVID-19) outbreak.

Having begun the month with markets looking fairly resilient in the face of a growing number of Coronavirus cases, stock markets eventually began to register a more pessimistic outlook. Despite a decent earnings season in both the US and Europe, coupled with ongoing strength in the macroeconomic environment in January, investors began to reassess both the severity of economic damage from the impairment of Asian supply chains and uncertainty over the spread of Coronavirus globally. The number of Coronavirus cases continued to grow through the end of February, with particularly severe outbreaks in South Korea, Italy, and Iran. Governments reacted with a mix of containment measures, public health warnings and fiscal measures to try and reassure citizens and financial markets alike in the face of mounting uncertainty.

In terms of historical context, the sell-off represented the largest weekly decline in shares since October 2008, and prompted a strong reaction from policymakers, with the Federal Reserve implementing an emergency rate cut of 0.5% in early March. Against this backdrop, core fixed income assets posted strong gains as recession fears increased. Inflation expectations and growth related commodity prices fell in line with growth expectations. In February the Chinese purchasing managers expectations fell to all-time lows as the economy came to an effective standstill, and economic data in developed markets began to show signs of the impact Coronavirus is having, mainly on supply chains and travel.

US

In the US Elections, former Vice President Joe Biden vaulted into the lead for the Democratic Party nomination, scoring big wins in the South Carolina primary and the 03 March Super Tuesday voting round. Macro-economic data in the US remained relatively strong, although early signs of the impact from Coronavirus began to show in the ISM (Institute for Supply Management) manufacturing numbers released in early March.

Europe

European growth remained subdued, even before the impact of the Coronavirus outbreak begins to register. On the political front, Germany's recent bout of political volatility showed little signs of easing as the Christian Democratic Union of Germany leadership contest began

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in earnest following the resignation of Annegret Kramp-Karrenbauer. The UK and EU continued to spar ahead of key negotiations regarding the future of UK/EU relations and European-policy makers also fretted over the heightened risk of immigration flows from the Middle East given instability in Syria and Libya.

Asia

In Asia, as well as the February Chinese purchasing managers expectations falling to all-time lows, other Asian countries such as South Korea and Japan also registered a deterioration in economic data as the business and consumer confidence took a hit from the Coronavirus outbreak.

Portfolio Management

Over the month, we reduced shares on the back of the continuing concern around the Coronavirus. We took a more defensive approach, reducing exposure to higher risk regions such as Asian emerging markets, Europe or Japan and increased our exposure to US shares which tend to be more defensive.

Portfolio diversifier's like government debt contributed positively to performance as sovereign bond yields declined after the sharp stock market sell-off driven by Coronavirus fears– prices rise as yields decline. Risk assets detracted from performance as business and consumer confidence were hit by fears of further economic disruption.

Outlook

We are reluctant to speculate regarding the future spread of the Coronavirus outside of what medical experts have forecast. We instead focused our efforts on measuring the potential economic impact of the measures taken (or likely to be taken) and following from that, the transmission channel to capital markets. At this early stage, our view is that the outbreak will need to worsen before we reach the point that policy makers feel compelled to take more meaningful steps towards fiscal and monetary easing. In the short-term that means higher volatility for stock markets and the potential for sharp drops as the market reacts to a constant barrage of Coronavirus-related headlines. In the medium-term, a strong economic rebound fuelled by pent up demand and loose policy will present opportunities to invest in certain sectors and regions at more attractive valuations. However, the timing is uncertain and the situation has the potential to meaningfully worsen before stabilising.

Given that we are in quite a mature phase of the economic cycle and assets are not cheap, we are aware of the increased likelihood of short-term price moves. Therefore, we will look to tactically reduce risk levels on our portfolios if indicators suggest further periods of heightened volatility are imminent. We also see some potential for return in pockets of the broader stock market and continue to find short-term opportunities across shares, bonds and currencies. Indeed, big movements in asset prices provide plenty of opportunities for dynamic asset allocation at the more granular sector, region and thematic level. That being said, it is our view that markets are in the latter stage of the cycle and finding the balance between return generation and downside protection will be the key to success for the rest of 2020.

Note: The Portfolio Investments and Atlas Portfolios are Multi-asset, globally diversified portfolios. Although the portfolios may share similar underlying investments in terms of asset and fund selection, they will differ in terms of the way the funds are managed and the proposition in which they are held. Please refer to the Key Investor Information Document (KIID) for details on the objectives of the individual funds. If you have any questions relating to specific differences of the Portfolio Investments or Atlas Portfolios fund ranges, please contact your Private Banker.

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