May 2020
Portfolio Review

So today sees the lifting of some restrictions and a gradual easing back to the new normal, whatever that will eventually be. I did smile at one commentator's response to the question "what does the easing of lockdown really mean?" to which the answer was that there are now plenty of beds available in Intensive Care units!

So are markets picking up with the same level of optimism as those embracing the end of lockdown? There have been positive developments over the course of May. Several countries have allowed restaurants and schools to reopen, travel restrictions are slowly easing and live sport is returning, at least to our televisions. Following the initial falls, the stock market recovery that started on 23 March, consolidated further making it either the most pronounced bear market rally in history, or that we have indeed already witnessed the turning point of the equity bear market that accompanies recessionary periods. It was also notable that the recovery broadened over the past week, with small cap stocks, markets beyond the US and cyclical stocks all finally enjoying a day in the sun as well. Despite the sobering evaluations of economic output in freefall, there was real optimism in the air that with the gradual and persistent reopening of western economies, the worst may be over and a strong recovery in sight.

But what has happened to concern over a second wave of COVID infections in the autumn, and a repeat of the extraordinary economic damage the lockdown has already inflicted? The market consensus appears to be that even if a second wave was to occur, a second round of lockdowns to the extent we have just witnessed would be unlikely. Either a vaccine will be available – at least to those groups shown to be most vulnerable – or a South Korea-style Track, Trace and Isolate regime will prevent the excessive damage of a full economic lockdown having to be repeated.

There is some logic in this argument, given that the working age population has only been marginally affected, continuously developing defence approaches and treatments are being introduced almost every week and for many reasons, there may no longer be the necessary public support for a second round of total lockdown.

Further, trends in the UK are heading in the right direction. Regionally there is variance but London, which was one of the regions hit first and at one stage was the national epicentre of the virus, has massively improved with research by Public Health England indicating the R value is just 0.4. There is every reason to believe this is replicable across the nation.

In terms of shocks, last month we touched on the WTI oil future briefly becoming negative. Since then, all major producers have significantly curtailed supply which has led to the market moving towards balance and inventories being drawn down, easing the capacity issues that led to the negative oil price in April. Demand is slowly picking up but it has been the supply cuts that have made the difference.

An increasing area of concern is the ramping up in tension between the US and China. The US has laid the blame for Coronavirus at China's door. China has denied this and has responded by increasing its grip on Hong Kong and passing a security bill, which makes it a crime to undermine Beijing's authority in the territory. This has been widely condemned by the West and the US has questioned whether Hong Kong has a wide degree of autonomy from the mainland and therefore should lose its special trading status and be treated the same as China under US law. This escalation has so far not materially impacted the market but it reminds the world that the two biggest nations are likely to rub against each other frequently.

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Elsewhere, European countries (including the UK) are aggressively pursuing fiscal stimulus to restart and reinvigorate their economies, rather than repeating failed austerity program approaches. Substantial government and central bank support is crucial in seeing the global economy through the current crisis. The European Commission has put forward a plan for a €750 billion (€500 billion grants, €250 billion loans) Eurozone recovery fund. This is notably bigger than the Merkel-Macron plan that had financial news outlets gushing before. Once the previous €540 billion package of April is added in, we are looking at fiscal stimulus worth up to 10% of GDP.

Fiscal action on the European front is particularly noteworthy because, until now, Europe's political setup has been notoriously obstinate and resistant to the idea of fiscal union. The Commission's offered solution is, as ever, a fudge of various measures rather than a comprehensive reform. But it is promising nonetheless. The Commission will now be able to call upon each Eurozone country to contribute 2% of its GDP towards a common budget and, crucially, it can use that future revenue as a guarantee to dip into bond markets in the short term.

Along the same lines, the Japanese government has approved a second supplementary budget for the fiscal year worth 6.2% of the nation's GDP. That brings Japan's total fiscal deficit for this year to 14.9% of GDP – the biggest stimulus boost in decades.

So whilst we still have no idea what the new normal will look like, there are grounds for optimism and the markets are responding accordingly.

Portfolios

Recovery across all portfolios has continued throughout May, with positive returns across all portfolios ranging from 2.04% gross to 5.16% gross.

Both Lindsell Train and Loomis Sayles generated significant positive returns in the region of 7%. This means the Loomis Sayles US Equity Leaders fund is now positive year to date with a gross return of just over 12%.

Over a twelve-month period, the Ethical portfolio is showing positive performance with a return in excess of 5% while most other portfolios remain flat. Traditionally referred to as ethical funds, these 'ESG' type investments have been very much in favour for over twelve months as consumers look to support businesses with a focus on Environmental, Social and Governance high on their list of core values. Seven of the top twenty performing funds, in May, follow ESG criteria in their investment mandates.

We commented on the underperformance of the H2O Multi-Returns fund during the initial market sell-off in March. In May, the fund returned just over 8% and whilst still negative year to date, has exhibited the recovery potential seen previously following a period of underperformance in December 2015. Held in conjunction with six other funds as part of a diversified returns element to portfolios, this has helped to lessen the impact of the decline.

In terms of volatility, In March the VIX index, a measure of volatility, spiked at 82 having held a long-term average of 15. Relative to the longer term, volatility is still high with the index currently at 29, however, we are seeing this progressively reduce to levels where we will be more comfortable to look at fund updates, given that time 'out of the market' could have a detrimental impact to investor returns.

All returns rounded and quoted gross of ongoing fees.
As always, please contact your adviser at Beckford James with any questions, or call the Head Office on 01225 437 600.