Marlborough Group

May 2020

Global Investment Commentary

SUMMARY

The impact of the COVID-19 pandemic continued to dominate markets, with an increasing focus on how countries would begin to relax their lockdown measures and the subsequent effect on the global economy. As the rebound in equity markets extended into May, volatility declined and the more moderate market moves compared to April suggest investors are in an observation period as the situation develops.

Market round-up

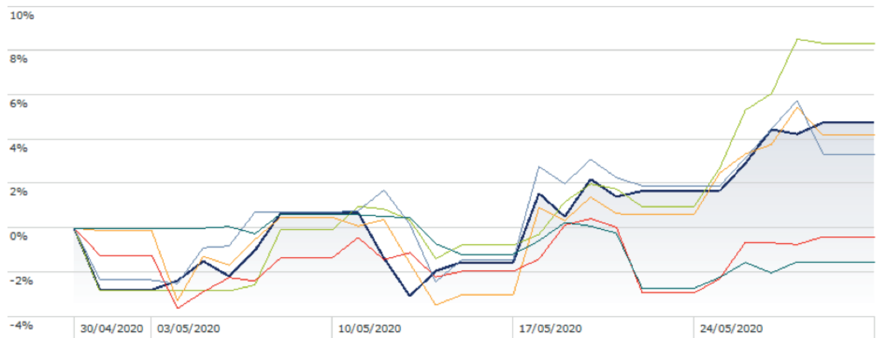
The infection rate in the UK remains high compared to other countries in Europe, where generally it has fallen significantly. Many states in the US began some level of reopening, though the daily infection rate has only fallen to around 65% of its peak in mid-April.

The S&P 500 climbed to end the month 4.76% higher and is now just 10% below the February peak. The FTSE 100 regained 3.34% while European and Japanese stock markets, which are typically more cyclical, also ended the month higher, up 4.19% and 8.34% respectively. The re-emergence of tensions with the US led to China's SSE 50 index declining by 1.53%, while the MSCI Asia Pacific Index crept up by just 0.40%.

Investors appeared to become somewhat more optimistic about the outlook after initial signs of success in human trials of a vaccine against COVID-19. However, despite the first steps being taken to exit lockdown and the positive news about a potential vaccine, it would be a brave call to predict with conviction how the public health outlook will evolve.

Growth stocks again outstripped their value counterparts and were ahead by more than 3.5% during the month. Developed markets

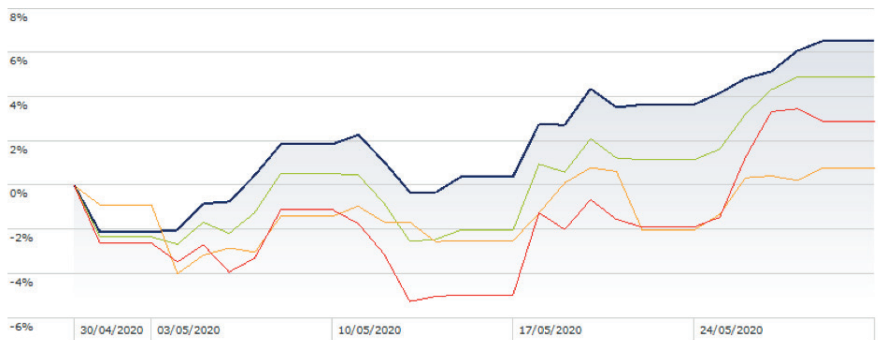
Performance - Major Indices



Investment Name	Value	Investment Name	Value
S&P 500 TR USD	4.76%	FTSE 100 TR GBP	3.34%
MSCI AC Asia Pac Ex JPN PR	-0.4%	MSCI Europe Ex UK GR EUR	4.19%
Nikkei 225 Average TR JPY	8.34%	SSE 50 A Share TR CNY	-1.53%

Source: FE, May 2020

Performance - Developed and Emerging Markets



Investment Name	Value	Investment Name	Value
MSCI World Growth GR USD	6.54%	MSCI World GR USD	4.9%
MSCI World Value GR USD	2.9%	MSCI EM GR USD	0.79%

Source: FE, May 2020

posted an aggregate gain of almost 5%, while emerging markets were up by just 0.79%.

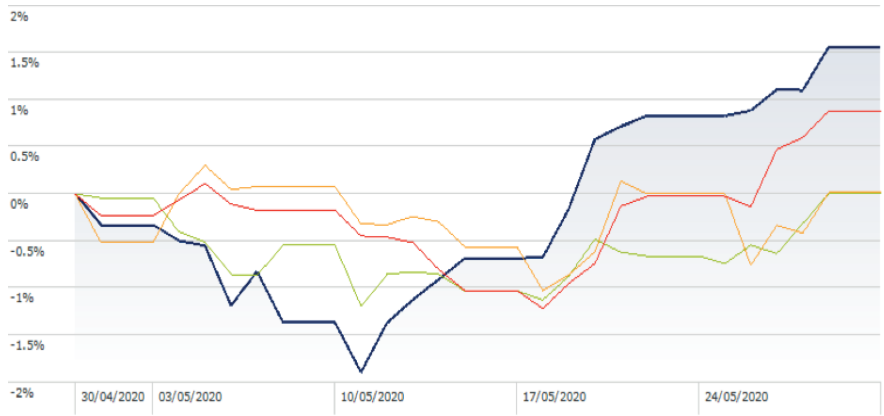
In bond markets, corporate bonds provided positive returns, while US Treasuries and UK Gilts flatlined as governments started to tally up the mounting cost of the crisis in terms of keeping economies afloat and stimulus to kick-start them again.

UK

The UK government announced further plans to continue gradually reopening more sectors of the economy. There has been no material increase in the daily infection rate but this will need to be monitored closely over the next couple of weeks.

First-quarter GDP in the UK fell by 2.0% compared with the previous quarter - the worst reading since 2008. The UK government's Coronavirus Job Retention Scheme, introduced to limit job losses, was extended to the end of October, though employers will be asked to share some of the cost from August. The scheme provides workers put on furlough with 80% of their salary (currently up to GBP 2,500 per month). The uptake of this scheme has been sizeable, with a recent Office of National Statistics survey showing that around 77% of businesses have applied. Despite this support, the claimant count rate, which looks at the number of people claiming benefits (largely due to unemployment), increased from 3.5% to 5.8%.

Performance - Fixed Interest



Investment Name	Value	Investment Name	Value
BBgBarc US Corp Bond TR U	1.56%	BBgBarc Global Treasury TR	0.00%
BBgBarc Sterling Agg Corp T	0.88%	BBgBarc Sterling Agg Govt T	0.02%

Source: FE, May 2020

Eurozone

The spread of the virus appeared to calm across the eurozone in May, with the daily infection rate roughly 90% lower than its peak at the start of April. Austria and Denmark appeared to lead the way in reopening their economies.

Much of the attention in Europe has been on a European Union-wide recovery plan. This would allow the European Commission to borrow EUR 750 billion in financial markets - equivalent to around 5.4% of the combined GDP of member states - to be funded by EU budgetary resources (contributions are based on a country's Gross National Income). The proposal is for EUR 500 billion of spending to be made available, mostly as grants, and to make EUR 250 billion of loans, which would be available to any EU country but focused on those most in need. This should help countries with already high debt levels, such as Italy, to access funding without having to issue more of their own debt.

Under the terms of its purchase programmes, the European Central Bank (ECB) bought over EUR 125 billion of government and corporate bonds over the past month. With the outline of a recovery fund announced by the European Commission, expectations are for an increase in the ECB's pandemic purchase programme at its next meeting on 4 June.

US

Economic data in the US has been particularly weak. The unemployment rate has recently reached almost 15%, the highest level in post-war history. With around 10 million additional people claiming unemployment insurance over the last month, the unemployment rate will continue to worsen in the next round of figures. The flash purchasing managers' indices showed that activity continued to weaken in May across both manufacturing and services.

With stay-at-home orders in the US having started around the end of March and activity still not back to full capacity, the expectation is for second-quarter GDP to be considerably worse than in the first quarter.

US corporate earnings reports for the first quarter of 2020 drew to a close in May and confirmed that earnings contracted by around 14% compared to the first quarter of 2019. More bad news is predicted with earnings for the second quarter expected to fall in excess of 40% year on year.

As the US economy shut down, consumer spending fell dramatically, despite increased purchases of groceries.

Almost all states have now relaxed their lockdown orders to some degree despite differing infection rates. As orders to stay at home are relaxed a close eye should be kept on the infection rate.

After the US Federal Reserve (the Fed) reacted quickly last month by increasing its balance sheet purchases, it made no meaningful adjustments to policy at its May meeting. The Fed's Chair did though signal a hesitance to use negative rates, particularly given some of the likely downside effects on the banking sector.

Emerging Markets & Asia

The number of reported cases in some parts of Asia has been trending down and economies are reopening, particularly in China and South Korea, where high levels of testing and contact tracing have been a key feature of their exit strategies. Falling numbers of cases in Japan are also a positive for the region. However, a large increase in cases in India and Brazil have put pressure on their economies and restricted gains in emerging market equities. Despite this situation, emerging market debt was the best-performing fixed income asset class in May, returning 5.9%.

Conclusion

There have been some positive signs and causes for optimism as containment measures have brought down infection rates. The focus of attention has been on the sense of relief as countries commence their lockdown exit plans and begin to show glimpses of increased activity.

However, while life in general may look like being on the road back to normality, economic activity during May suggests that economic data for the second quarter is likely to be worse than the first. While central bank and government interventions have softened the considerable blow, if and how companies can navigate the crisis and when the working population can return to employment will be the measure of a successful recovery.

With such lingering uncertainty and the potential threat of a second wave of infections if countries have been too quick to reduce restrictions, we continue to remain relatively neutral in terms of high-level asset allocation. The key to individual equity and fixed income selections will be finding companies that are positioned to benefit from an upturn, while also having the financial strength to survive another shock.

Economic Projections (31/05/2020)

Economic Growth

Country/Region	Real GDP YOY Growth (%)		
	2020	2021	2022
UK	-7.80	5.50	2.70
USA	-5.70	3.90	3.00
Eurozone	-7.60	5.00	1.80
Germany	-6.20	4.90	2.00
France	-9.00	6.00	1.80
Japan	-4.90	2.20	1.20
China	1.70	8.00	5.50
India	4.30	-1.90	7.10
Asia	1.30	5.80	5.30
Emerging Markets	0.00	5.20	4.90

Source: Bloomberg

Interest Rates

Country/Region	Central Bank Interest Rates (%)		
	2020	2021	2022
UK	0.10	0.10	-
USA	0.25	0.40	-
Eurozone	0.00	0.00	-
Japan	0.00	0.00	-
China	4.20	4.15	-
India	3.60	3.75	-

Source: Bloomberg (Bloomberg forecast currently unavailable for 2022)

Foreign Currency Exchange Rates

Currency Pair	Exchange Rate		
	2020	2021	2022
GBP/USD	1.27	1.33	1.38
EUR/GBP	0.88	0.87	0.85
EUR/USD	1.12	1.16	1.19
USD/JPY	107.00	109.00	107.50
EUR/JPY	119.00	124.50	127.00
USD/CNY	7.00	6.90	6.60
USD/INR	74.87	73.25	72.00

Source: Bloomberg

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