Realm Investment Management Market Update - April 2020

For those who regularly follow our market updates you will note that we last reported in early February. Since then of course, the world has witnessed a global pandemic, the severity of which has effectively closed the world economy. Nothing in our lifetime (save for the few who lived through the tail end of World War II) comes remotely close to the impact that this has had on our daily life.

Yet when compared to previous stock-market declines, and in many ways' indicative of the crisis we all face, is that when chatting to clients we note that there is a general sense of calm. Whilst we are entirely focused on investment markets and concerned to protect your investments, we are acutely aware that we all face a more immediate challenge, notably life itself.

OUR MACRO VIEW

Most analysts accepted at the start of the year that we were late in the business cycle but none of them foresaw the global economy grinding to a halt caused by the spread of the coronavirus. Investment markets are of course a collective reflection of the view that investors have of global events and their effect upon economies. Hence it is no surprise that markets, focused entirely on the ramifications of the coronavirus.

When the markets confronted this extraneous event, which could not be quantified in terms of its effect and duration upon economies, they reacted very swiftly in attempting to assess the risk. Markets did this by discounting prices as rapidly as possible trying to find a comfortable valuation. The market's reaction was severe and as a result March broke many records as commentators struggled to find suitable comparisons.

In actual fact the movements were huge in all directions. Equity markets initially fell by approximately 40% from their height in January, most of the movement happening within 10 days and then recovered by an 20% from their lows in an astonishing 4-day period. Volatility, as represented by the VIX (often called the "fear gauge") was extreme, spiking to its highest ever level. To illustrate just how extreme volatility has been, even within the bear market that is currently being played out, the Dow Jones Industrial Average managed to have its best day since 1933 on March 24th, and from there its best three-day rally since 1931.

A recession now seems inevitable and the debate has started as to how long it will last and how deep it will be. The question, from an investment perspective, is how bad an economic scenario has the markets already factored in? From what we can see the markets are currently pricing in the worst-case scenario. Should events prove less catastrophic and the world resurfaces with less economic damage than expected, then investment markets should rally from here though such an outcome could be several months away.

In historical terms, March was an incredible month in that the central banks responded in an unprecedented fashion, cutting interest rates and restarting quantitative easing whilst at the same time governments around the world announced huge fiscal stimulus plans to financially support their people and domestic corporations.

NORTH AMERICA

In the U.S. leading economic data for March hit an all-time low with the effects of coronavirus on manufacturing and services. The U.S. now has more confirmed cases of COVID-19 than China with recent data showing a massive spike in U.S. jobless claims of over six million people filing for unemployment benefits.

To illustrate the extent of the stimulus, the US announced a funding package amounting to more than $2 trillion to support the economy through this crisis. This was the biggest fiscal stimulus bill ever passed. The result of which is that the US Central Bank will start buying an equivalent amount of bonds each day that they were buying each month during the last global financial crisis.

In the last few days it has been rumoured that President Trump will announce further stimulus plans to protect the US economy with the likelihood that other economies will follow suit.

EUROPE

As infections and deaths rose sharply through Europe, severe restrictions on movement were announced in many countries. Manufacturing and services saw the largest monthly fall since July 1998 with jobs being cut at the fastest rate since 2009. Many economists are predicting the sharpest recession in Europe for decades. In response, the European Central Bank launched PEPP, Pandemic Emergency Purchase Programme, and gave the commitment that this would be "as much as necessary and for as long as necessary" to protect the economy.

UNITED KINGDOM

The U.K. put in place strict emergency measures and a massive financial support package for both businesses and employees. Conference centres were requisitioned to be used as care centres for the critically ill. Boris Johnson confirmed he had tested positive for the coronavirus although his symptoms were mild and would continue leading the government while self-isolating.

The Bank of England announced a further cut to interest rates bringing them down to just 0.1%. This is the lowest ever recorded interest rate decision. At the same time, they announced an additional £200 billion asset purchasing programme to further ease liquidity concerns. Government bonds, including UK Gilts, were fiercely volatile but made net gains over the month. Corporate bond prices fell with concerns about corporate profits and not surprisingly higher yielding, lower rated bonds were the worst hit as investors sought safer returns.

OIL PRICE

Stock-markets are also having to adjust to a massive oil price shock following the breakdown of an agreement between OPEC and Russia over oil production targets. The result of which has caused both countries to dramatically increase supply.

The fall in the oil price was accentuated by the collapse in industrial demand as industries were forced to close through both lack of trade and government measures. One of the most visible areas was obviously travel where airlines have virtually ceased operations after reporting 80% declines in sales and facing closure and restrictions of major airports, including Gatwick and a part of Heathrow.

This worsening supply/demand imbalance has forced a historic collapse in the price to a level which is uneconomic for many producers and threatens a serious rationalisation of the industry.

Further negotiations are planned for June, though there have been attempted interventions notably by President Trump which, as of yet, have not resulted in any progress.

MARKET CHARTS

Our Market Charts for the U.K. and U.S. stock-markets are shown below. These represent a monthly, or longer-term view.

The Breadth indicator on the U.K. chart stayed negative (red) in March, and our Momentum indicator, which is in negative territory, ticked down.

On our U.S. Market Chart through end of March the Breadth Indicator also stayed negative (red) and our Momentum Indicator, although still positive, ticked down.

SUMMARY

Investment Markets will continue to trade and though the corporate landscape may change with many of today's industries such as tourism, airlines and oil producers adversely affected, there will be other winners as the world adapts to a new era.

Invariably there will be certain sectors where winners will emerge, be that in Bioscience, Technology and Healthcare. Other industries will regain their operational functions as is now evident in China and the Asian regions, where production capacity is approaching 90% of pre-coronavirus conditions.

Strategically, rather than second guess forecasts at this very early stage we plan to use pricing opportunities to reposition our investment portfolios into areas which present solid secular growth prospects as some of the sectors highlighted above would indicate.

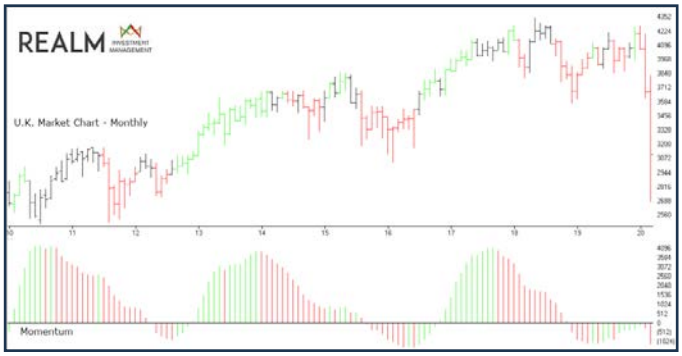
In time we can expect that the spread of the virus will finally abate and daily routines will return to some sense of normality. Investment markets, as they are prone to do, will likely pre-empt the economic recovery and so we would hope stock-markets, as well as bonds, will once again start to rise in value.

To this end, we are closely monitoring the prospects for all investment categories and would anticipate the need to redistribute our investment portfolios in order to enhance the investment return.

We hope you have found this latest update of interest. Thank you for reading.

Further weekly research can be found here.

U.K. MARKET CHART - MONTHLY



U.S. MARKET CHART - MONTHLY