February Market Reflection

| 2 March 2020 |

Investors entered 2020 in a relatively upbeat mood, thanks to an improving outlook for global economic growth. This was largely a result of a ceasefire in the tariff war between the US and China, combined with increased liquidity provision by central banks. However, the world has suffered a rude awakening in the last month owing to the outbreak of a SARS-like virus which leads to a condition now labelled COVID-19. Initially this was mainly contained within the Chinese province of Hubei, and there was some optimism that the negative effects on both supply chains and consumer demand would be relatively short-lived. Indeed, egged on by lower bond yields and the prospect of lower interest rates, investors bid several equity market indices up to new all time-highs, even as recently as 19th February. The tide turned rapidly following a sharp escalation of new cases in Northern Italy. With that, a reassessment was made of the potential further spread of the virus and of the negative economic consequences, leading to more intense selling of risk assets. As has been noted in recent market sell-offs, a lack of market liquidity can tend to exacerbate such moves, and the current case is proving to be no exception. Quite where markets find support is difficult to pin down. However, there is some consolation to be taken from three factors: first, growth trends were improving before the virus broke out; second, central banks are fully supportive; third, there is increasing discussion of greater government spending, notably involving projects that can be seen to counter the threat of climate change. All of these should prevent a correction turning into something materially worse. Meanwhile, balanced portfolio investors are reaping the benefits of holdings in safer assets including government bonds and gold.

- Global growth decelerated in 2019, and any expected recovery in 2020 appears to have been dashed by the outbreak of the coronavirus.

- Analysts' corporate earnings growth forecasts of around 10% at the start of the year have yet to be materially reduced. However, another year of zero aggregate growth, at best, is in prospect.

- Bond yields have hit new all-time lows in several countries as investors seek havens for their cash. The US 10-year yield is now just 1.17%. The 10-year UK Gilt yields 0.39%, and the German 10-year Bund minus 0.61%.

- Fiscal stimulus is being more widely touted as a policy lever to encourage higher rates of growth. The extremely low government bond yields mean that cheap capital can be provided for projects that have the potential to boost productivity and to combat climate change.

- The UK might have left the EU, but Brexit is far from resolved. The government continues to negotiate trade terms with the EU, but there remains a risk of no deal being reached at the end of year. This has resulted in the pound giving up its post-election gains.

- In the US, the focus has been on the Democratic Party primaries. The front-runner is currently Senator Bernie Sanders, who is the most left-wing of all the candidates. Should he win the nomination, it would increase the threat of tax rises and tighter regulation, especially of the technology sector, should he then go on to win the election. For now, though, Donald Trump remains the favourite.

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