July Market Reflection

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The equity market recovery stalled in July in the face of deteriorating news on the number of new Covid-19 cases, notably in the sunbelt states of the United States. This was exacerbated by renewed, but localised, outbreaks in parts of Europe. Thus, although the initial rebound in economic activity from April's trough has been very sharp, even "V"-shaped, concerns of a more protracted full recovery are in the ascendant once again. A key factor will be employment levels. Although furlough measures have contained the rise in official unemployment rates in much of Europe, several high-profile companies have announced permanent job cuts, and more are expected to follow. Countering the threat are fiscal stimulus packages and continued central bank support. On this front, the European Union's creeping progress towards the implementation of a €750bn stimulus package is a positive development, while the US Congress continues to argue about the scope and scale of its own latest stimulus. Even so, both are expected to proceed given the current imperative to support economic growth. Central banks are more in the mode of maintaining policies rather than introducing new initiatives, but appear committed to extending very loose monetary conditions well into the future. This stance has been acknowledged in bond markets, where yields on 10-year sovereign bonds in both the US (0.54%) and the UK (0.07%) have hit all-time lows. Burgeoning government and central bank balance sheets also raise the threat of future inflation, and that has catalysed a resurgence in the price of gold, which has made new all-time highs, and silver. The latter is also seen as a play on new green-economy initiatives.

- The IMF's latest forecast sees the global economy shrinking by 4.9% in 2020, followed by a recovery of 5.4% in 2021.

- Much depends on the evolution of a vaccine. Investor surveys point to expectations of one being readily available within six to eighteen months.

- Global earnings are forecast to halve in 2020. However, initial results for the second quarter reporting season have, on average, beaten analysts' reduced expectations.

- The US presidential election looms large, with Democratic Party challenger Joe Biden ahead in the polls. Although his more left-leaning policies might normally instil fear in investors, that is balanced by the fact that he is viewed as having a safer pair of hands than the incumbent.

- The US Dollar has given up almost a tenth of its value on a trade-weighted basis since its peak in March. US interest rates now offer little premium versus other developed market currencies, and the impact of the virus could lead to a weaker economic recovery in the US than elsewhere.

- UK stock market dividend payments are projected to be less than half of 2019's level this year, although there is scope for a meaningful recovery in 2021 as banks are expected to be able to resume payments.

- The biggest question facing investors in the medium term concerns the potential re-emergence of inflationary pressures owing to policy stimulus measures and possible supply chain disruption. This would change the investment landscape dramatically following four decades of persistent disinflationary trends.

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