October Market Reflection

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Equity markets were unequivocally positive in August and equally negative in September, but October turned out to be, in footballing parlance, a "game of two halves". The drivers, as so often recently, were Covid developments and the build-up to the US Presidential election. On the former subject, investors entered the final quarter of the year on an upbeat note. Covid cases around the world appeared to be relatively stable, and optimism about the approval of one or more vaccines before Christmas was evident. However, as the month wore on, Covid case numbers started to accelerate once more. Even though mortality rates remain well below those of earlier in the year, the threat of healthcare systems being overwhelmed became a reality once more owing to the sheer volume of new infections. This, in turn, has led to more social restrictions and the associated loss of economic activity, snuffing out an incipient rally in more economically sensitive stocks. Positive new vaccine news has also been slow in arriving. As for the race to the White House, Democratic challenger Joe Biden, the market's preferred choice, held a strong, double-digit polling lead well into the second week of October, raising hopes of a "Blue Wave" victory, in which Senate control, along with existing control of the House of Representatives, would allow the swift passage of a multi-trillion dollar stimulus package in the New Year. As the polling gap narrowed in the approach to Election Day, both nationally and in critical battleground states, investors decided that profit-taking was the best course of action. Even so, markets display little of the panic evident earlier in the year, and it is clear that both fiscal and monetary support will remain available should the need arise. While increased volatility is to be expected in the short term, many of the uncertainties should be resolved within a matter of weeks.

- The IMF's latest forecast sees the global economy shrinking by 4.4% in 2020, followed by a recovery of 5.2% in 2021. Emerging Markets will lead the recovery, led by China.

- Expectations for a widely available Covid vaccine continue to centre on the first half of 2021. Any slippage in the timetable would be of concern.

- The third quarter corporate earnings season has begun well, with a substantial majority of companies beating forecasts. Banks, in particular, have benefitted from a strong trading environment and reduced bad debt expectations. There is growing potential for the resumption of dividend payments in 2021, subject to regulatory approval.

- Brexit negotiations continue past original deadlines. This suggests, perhaps contrary to appearances, that both sides would prefer to sign a deal rather than forcing the UK to have to conduct trade under the World Trade Organisation tariff structure. A resolution might not be reached until the second half of November.

- Government bond markets have remained relatively calm in the face of increased equity market volatility. Threats of increased supply to fund fiscal stimulus packages put upward pressure on yields, but this continues to be balanced by central bank purchases. Both the Bank of England and the European Central Bank are expected to expand their asset purchase programmes in December.

- Investors continue to be on the lookout for signs of higher inflation. Although it is apparent in specific areas, it remains generally subdued in all regions, despite efforts to create it.

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