Wealth Management
Weekly Market Update

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Market Update

UK equities were down nearly 9% this morning, with the natural resource and banking heavy indices experiencing weakness for three prime reasons. First, coronavirus fears continued to rise as Italy quarantined 16 million residents, with investors fearful of this impact on the global economy and consumer sentiment. Secondly, Russia's refusal to follow suit with regards to new Oil supply cuts has ushered in a new price war among major producers, which, paired with an expected decline in demand, saw Oil prices plunge 30%. As a result BP and Shell have seen sell-offs greater than 20% in magnitude. Thirdly, on declining bond yields (which tend to decrease net interest margins) and greater recession expectations, Barclays and Lloyds shares sold off sharply. US stocks closed last week down -1.2% in GBP terms last week, with the best performing sectors being those more defensive in nature, namely, Utilities, Consumer Staples and Healthcare. In the FX markets, the Pound rallied +1.8% versus the US Dollar, however this was more of a function of the weaker Dollar in light of greatly enhanced Fed cut expectations, with Sterling falling versus the Euro and Japanese Yen. Bonds have seen continued demand even as yields have fallen to historic lows. The UK 2Y Gilt yield turned negative this morning, and credit spreads continue to climb across the globe, especially for HY issuers, many of whom are in the oil & gas business. In the flight to safety Gold rallied +5.6% last week.

UK Stocks	US Stocks	EU Stocks	Global Stocks	EM Stocks	Gilts	GBP/USD	Implied probability of a rate cut at the next Fed meeting
▼ -1.6%	▼ -1.2%	▼ -1.3%	▼ -1.4%	▼ -1.2%	▲ +3.4%	▲ +1.8%	100%

all returns in GBP to Friday close

Macro News

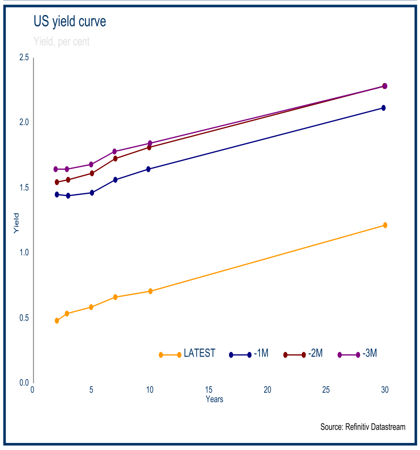
- The Federal Reserve announced an emergency half-point (0.5%) rate cut, citing "evolving risks to economic activity" from the coronavirus. In a unanimous statement from the Fed's Open Market Committee, the members declared "the fundamentals of the US economy remain strong" and the move came after G7 finance ministers and central bank governors pledged to take "all appropriate policy tools" to maintain the economic health of the advanced world.
- The US economy hired 273,000 people last month – nearly 100,000 more than the consensus forecast. Job gains recorded were the highest since May 2018. Wages rose as well and the unemployment rate dropped to 3.5%, a 50-year low.
- Chinese PMIs dropped to the lowest levels ever reported. The official NBS Manufacturing PMI fell to 35.7 while the services PMI fell to 29.6, as the country was faced with quarantine conditions and travel bans in February.

The Week Ahead

- This Wednesday the UK budget will be delivered by Rishi Sunak, just four weeks after he became chancellor. Markets expect that the budget will address the economic impact of the coronavirus and will also address the tax commitments from the Conservatives' manifesto.

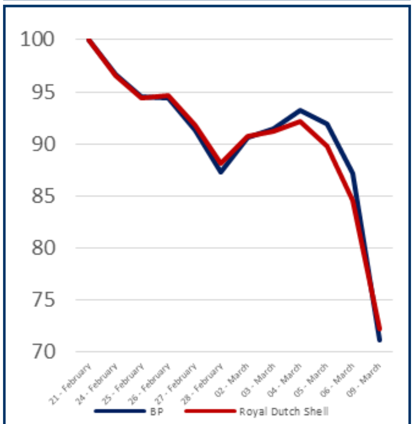
Week in Charts

Fig 1: US Yield Curve Shifts Down



Over the weekend, for the first time ever, the entire US yield curve traded below 1% in a display of the extreme risk-off sentiment in markets. US Treasuries are seen as a safe-haven assets for investors and so yields fall when investors are nervous about markets and the economy.

Fig 2: UK Oil Companies Suffer



Source: Mazars Calculations

The largest Oil price fall since the 1991 Gulf War of 30% has been due in part to a disagreement on production cuts between Russia and Saudi Arabia. BP and Royal Dutch Shell (the second and third largest UK listed companies by market capitalisation) have fallen 25% and 22% respectively this morning.

View From the Desk

The market downturn due to the coronavirus continues unabated, despite rate cuts and pledges of fiscal support measures. As of early Monday morning, the S&P 500 was down a further 140 points, roughly 17% below its February 19 highs. US Treasury yields, a very reliable fear gauge, have dropped to all-time lows. As time has passed, the more our "this is one of those things" thesis is challenged. This will be the fourth straight week of negative market returns and the worst downturn since December 2018, however that fall took place over the space of three months. We are not so much worried about the speed of this move, as algorithmic trading tends to exacerbate both the breadth and velocity of downturns. Instead, we look back to our thesis, that this is a Secular Stagnation economic environment, where risk asset prices are propped up by central bank-driven financial repression. Instead of looking for catalysts for a return of fundamentals, we have been actively looking for scenarios where central bank printing does not work anymore. While Covid-19 looked like a possible "Black Swan", the truth of it is that the virus is much less deadly than SARS, MERS or Ebola. Yet it has caused significantly more damage to financial markets. Why? We believe it is a confluence of runaway market prices and simple fear. When, in late January, pictures of people hunted by drones and chased with nets in Hubei province made the news, it seems they had an impact on our collective sentiment. We rushed to supermarkets, cleaned out sanitary perishables and prepared for the worst. We significantly cut down consumption in discretionary services such as travel, restaurants, movies etc. As consumers drew up their battle plans, so did governments, who took their cue from China without much hesitation and some are now quarantining entire provinces. Lombardia in Northern Italy is officially on lockdown, much like Hubei in China, and others could follow. The sharp and simultaneous downturn of global economic and financial indices is reminiscent of 2008-9, and businesses are already facing liquidity issues. QE might be the most effective central bank tool as it is money immediately directed to risk assets, as opposed to rate cuts which constitute merely an opportunity for leverage. What will it take to stop the economic and financial slide? We believe that governments and central banks may well try a combination of aggressive fiscal easing and more monetary easing in the next few days. The UK budget on Wednesday may provide an interesting litmus test on that strategy. Ultimately, the ability of central banks to solve problems will once again be tested, against a financially unconventional enemy: real fear. Our base case scenario is that fears are overdone and markets should respond to aggressive stimulus. If, however, the measures taken in the next few days fail to calm markets, then investors should consider the real possibility that the 11-year economic and financial expansion may come to an end.

David Baker, CIO

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