MERRION INVESTMENT MANAGERS

CANTOR Fitzgerald

Strategy & Outlook MARKET UPDATE

July 2020

June

Global equities pushed on further in June, rising by 1% on the month to finish one of the best quarters in the last 50 years (+15.3%), though still 7.2% lower year-to-date after the collapse of the first quarter. Continued positive news on reopening of economies, a larger than expected fiscal stimulus from Germany (4% of GDP), a significant increase in the ECB's stimulus measures (an extra 600bln of quantitative easing and an extension of the term), rumours of a further fiscal package in the US (another $1tln) and a huge positive surprise in US job numbers combined to lead to a continuation of April and May's surge in equity prices in early June, the US market briefly getting into positive territory on a year-to-date basis.
However, this coincided with two note-worthy events as both the odds of a democratic clean sweep in November and the number of coronavirus cases in US states bordering South America rose to unsettling levels. Further disappointment in regards to the potential for European banks paying dividends in the near term, continuous Brexit stalemate ahead of the month end deadline and a Fed meeting which couldn't deliver anything new all contributed to a sudden change in sentiment, culminating in a large global sell off mid-month, after which equities struggled for direction as the continued reopening globally is met by a very concerning spike in Covid-19 cases (and hospitalisations) in the US and South America, no progress on Brexit talks and ongoing deterioration in the US-China relationship.

The resumption of the spread of the virus questions the speed at which the US economy is reopening, forcing the governor of Texas to pause the reopening there and a number of large companies to either close businesses again or delay reopening. Outside the US outbreaks in Germany, the UK and China have forced authorities to reimpose lockdowns on a localised basis.

On a positive note, apart from the very strong employment report in the US, retail sales also rebounded very strongly, indicating that the government's measures to support the unemployed have worked. However claims for unemployment in the US remain stubbornly high, indicating that a further fiscal package of some sort will be required, as the emergency relief programme runs out at the end of July.

As one of the strongest quarters for global equities in almost 50 years draws to a close and having been positioned at the upper end of our growth asset ranges for all of it, we reduced exposure over the last 2-3 weeks as a technically vulnerable market at elevated valuations met a murky short term macro-economic and geo political outlook. Within defensive assets, we also took profits on some of our corporate bond holdings which have performed so strongly since mid-March. Although the Federal Reserve will continue to support this sector, yields have fallen so much that valuations are no longer as attractive. Funds are now positioned closer to neutral, but with downside protection in pace via our alternative strategies.

Outlook

We continue to have a very positive outlook for equities over the medium term as a zero-rate world and co-ordinated global fiscal expansion will drive investment into the industries that will dominate the next decade. However, after the strong rally off the March lows our short-term risk indicators have begun to flash orange. The surge in cases in the US raises some questions about the pace of reopening and the speed of recovery. Meanwhile, the US-China situation continues to deteriorate, as does the overall backdrop in emerging economies where we have concerns about rising Covid cases, the lack of tourism, declining FX reserves and excessive external debt. Together with a divisive US election where the challenger appears to have a lot less market friendly policies than the incumbent, these factors have the potential to generate further short-term volatility over the summer, which will provide better opportunities to exploit our more medium term view. The continued benefit of our active approach, driven by a strong coherent and well-tested investment process should be evident over the course the 3rd and 4th quarter of this year.

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