Market Brief

September's highlights

- Led by declines in big US tech stocks, global equity markets handed back at least some of their quarterly gains in September. Global credit spreads rose while UK gilt yields fell over the month and US treasury yields were little changed.
- A rapid resurgence of COVID-19 infections in Europe became increasingly apparent leading to a re-imposition of some localised lockdown restrictions.
- Oil prices fell close to 10% in September on fears of the impact on demand from renewed restrictions and Gold slipped back from record-highs with the dollar spot-price falling 3.4%.
- There was a meaningful move lower in Sterling in September, with a lack of progress in Brexit negotiations the most likely explanation. Meanwhile, the US dollar reversed some of its recent weakness amid a return of volatility and risk aversion.
- After having risen to 1.0% in July, headline UK CPI inflation fell to 0.2% in August, its lowest level since December 2015.
- Purchasing Managers Indices and high frequency data still point to continued recovery in Q3 but suggest its pace slowed towards the end of the quarter.

Q3 Update

Market Performance

UK	Q3 20*	Q2 20	Q1 20	GLOBAL	Q3 20*	Q2 20	Q1 20
EQUITIES	-2.9	10.2	-25.1	**EQUITIES**	7.0	18.4	-20.0
BONDS				North America	9.3	21.2	-19.6
Conventional gilts	-1.2	2.5	6.3	Europe ex UK	2.1	15.4	-20.9
Index-linked gilts	-2.2	10.3	1.6	Japan	4.8	11.8	-17.2
Credit	1.2	7.0	-3.4	Dev. Asia ex Japan	2.7	14.8	-20.6
PROPERTY**	0.3	-2.3	-1.4	Emerging Markets	8.7	17.6	-20.2
STERLING				**GOVERNMENT BONDS**	0.4	1.0	3.2
v US dollar	4.6	-0.4	-6.4	**HEDGE FUNDS*****	4.4	6.2	-9.0
v Euro	0.2	-2.7	-4.2	**COMMODITIES**	10.4	12.4	-25.6
v Japanese yen	2.3	-0.4	-7.0	**Oil**	-0.6	82.5	-65.9

Percentage returns in local currency ($ for Gold and Oil). *All returns to 30/09/2020, apart from property (31/08/2020).

- Equity and credit markets rose in Q3 amid a post-lockdown rebound in economic activity, a better than expected earnings season, optimism over vaccine trials and declining COVID-19 infections in the US and Europe. However, political uncertainty, on both sides of the Atlantic, and a resurgence of COVID-19 infections saw markets slip back in September. Nonetheless, global equity markets produced strong positive total returns over the quarter while sovereign bond yields rose, and credit spreads moved well below end-June levels.

- GDP data will likely reveal record-breaking growth rates for many economies in Q3, following Q2's record-breaking declines. However, while high frequency data, such as travel and navigation app usage, point to a continued recovery in activity in the major advanced economies, they suggest the pace of improvement slowed markedly towards the end of Q3.
- Full-year forecasts for global GDP growth appear to have passes their nadir but most advanced economies are not expected to return to pre-pandemic levels of output for several years. September's Consensus Forecasts point to a 4.6% fall in global GDP in 2020 to be followed by a 5.0% expansion in 2021, largely owing to the secular momentum of the Chinese economy
- Composite Purchasing Managers' Indices, which combine manufacturing and services, signalled the recovery in global activity continued in September. Regional indices generally remained at levels consistent with month-on-month expansion, though did point to more moderate expansion in some regions. The labour market continues to improve in the US, albeit at a slower pace. While job markets had initially remained more resilient in Europe and the UK, job cuts are accelerating and may face further pressure as government support schemes are scaled back.
- Second waves of COVID-19 are increasingly evident and though mortality rates have fallen, this may simply reflect increased testing capturing milder and asymptomatic cases. Infection rates are rising rapidly in Europe, particularly in the UK, Spain and France, whilst other economies, such as Latin America and Southern Asia, are yet to see an end to their first wave. However, most countries appear keen to avoid the large-scale national lockdowns seen in the first two quarters.
- UK CPI inflation reached its lowest level since December 2015 in August, falling down to 0.2%, below flat expectations, having reached 1.0% in July. The main drivers behind this were the fall in restaurant and café prices following the government's 'Eat Out to Help Out' scheme. Lower air fares and clothing prices also put downward pressure on inflation over the month.
- The Fed's shift to "flexible" average inflation targeting likely means interest rate rises are even further away than previously envisaged. The Bank of England continues to send mixed messages on the potential use of negative interest rates, but an operational review is ongoing and market pricing, at least, suggests negative interest rates may be introduced 2021.
- US 10-year treasury yields were little changed, ending the quarter at 0.68% p.a. Equivalent UK yields rose 0.06% p.a. to 0.23% p.a. while German bund yields drifted 0.07% p.a. lower to -0.52% p.a. Equivalent Index-linked gilt yields edged below end-June levels resulting in a rise in 10-year implied inflation to 3.3% p.a.
- Despite rising towards the end of the quarter, global investment grade credit spreads fell from 1.6% p.a. to 1.4% p.a. and global speculative-grade spreads fell from 6.4% p.a. to 5.6% p.a.

Defaults continued to rise but have so far mostly been contained in the troubled US energy and retail sectors. Meanwhile, expectations for peak default rates eased over the quarter as supportive market conditions has allowed companies to raise new finance, bolstering their ability to navigate the downturn.

- The GBI-EM Traded Index returned 0.6% in dollar terms reflecting a marginal fall in yield which was partly offset by a fall in the in the major index currencies, in aggregate, versus the dollar. Hard currency debt returned 2.3%, primarily driven by a fall in spreads from 4.9% p.a. to 4.4% p.a., as treasury yields were little changed.
- Despite a return of volatility in September, global equity indices produced a total return of 7%. Even though US tech stocks were at the heart of recent declines, the US region once again out-performed and the UK was again a stand-out underperformer. Emerging markets also outperformed, helped by a strong rally in Chinese equities early on in the quarter.
- With regards the sectoral pattern of performance: with the exception of oil & gas and financials, cyclical stocks generally outperformed more defensive stocks. Technology once again outperformed, extending its large year-to-date lead at the top of the performance rankings while oil & gas massively underperformed, cementing its place at the bottom.
- Despite slipping back in September as trade talks faltered, sterling still partially reversed some of its losses of the first half of 2020, rising 1.7% in trade-weighted terms since the end of June. Even allowing for September's gains, the US dollar fell 2.8% in trade-weighted terms in Q3. The dollar's losses have mostly been against advanced economy currencies, unwinding the gains of March and April amid an easing of global risk aversion and narrowing interest rate differentials.
- The rolling 12-month performance of the MSCI UK Monthly Property Index continues to fall and is now -2.9% to the end of August. Capital values are, in aggregate, 7.9% lower over the same period This is predominantly due to a 18.9% fall in capital values in the retail sector over the last year, but values in the office and industrial sectors have also fallen 3.7% and 1.3%, respectively. Material uncertainty clauses were removed from the vast majority of the UK property market in September, reflecting valuers increased confidence in valuations amid increased transaction activity.

For and on behalf of Hymans Robertson LLP

Additional Notes

Risk Warnings

Please note the value of investments, and income from them, may fall as well as rise. This includes equities, government or corporate bonds, and property, whether held directly or in a pooled or collective investment vehicle. Further, investments in developing or emerging markets may be more volatile and less marketable than in mature markets. Exchange rates may also affect the value of an overseas investment. As a result, an investor may not get back the amount originally invested. Past performance is not necessarily a guide to future performance.