All eyes on the 4th July

One of the many things I enjoy about my job is speaking with my clients. This enables me to get a sense of perspective whilst making recommendations and taking account of high-profile fund managers and economists views concerning the global outlook.

There has certainly been a change in sentiment this week within the markets. A more subdued mood after plans to loosen the current restrictions from 4th July raised further fears of a second spike. This fear accelerated following the exceptionally warm weather that led many people to the beaches, causing overcrowding and sadly, vast amounts of litter and debris.

A second spike will certainly be a step back and the emotional consequences of returning to isolation will challenge the most positive of views for the rest of the year ahead. We know we are going to be living with COVID-19 for a while, but the key is not only how the government tracks and traces the spread, it will also be how the government stamps down or isolates the problem at a local level. Policing will be a separate challenge, with scuffles that have been reported at street parties throughout the UK.

If we predict another spike and believe there are going to continue to be challenges over the coming months for the markets, then why are we not de-risking client portfolios?

The issue here is, there is no perfect solution, cash will provide poor returns over the medium to longer term and it is difficult to catch the markets at the bottom. If a credit crisis appears, then cash could expose clients to higher levels of risk by being defensive. Fixed Interest products such as Sovereign and Corporate debt instruments are often the chosen solution in a falling market, however there are also concerns over liquidity, which could impact on the interest payments and ability to exist from them, should everyone decide to do so, typically experienced when there is the likelihood of interest rate rises.

We have rebalanced portfolios since the pandemic and feel comfortable they sit well in the current environment and outlook. That said, our next portfolio review takes place next week which will enable us to track the changes made, the impact they have made on performance and volatility.

During one of my scheduled video-based client reviews, I said to my clients, "it is hard to time the markets and we could get it wrong, so damned if we do, and damned if we don't". It was at this point I learnt my newest acronym, TINA. This was used to express their feelings in connection with their portfolio. At the moment, "There Is No Alternative (TINA), all options have risks, we are best to remain in the markets, our objectives remain unchanged and we need to hold the capital somewhere, so why not where it is currently". This is a simple but very effective statement in my opinion.

There is a lot of noise once again about the how the current pandemic is impacting the UK. An interesting feature of the pandemic, with potential investment implications, is the tendency for economic crises to hit different social groups in different ways.

This was true in the early 1980s recession, which focused on heavy industry and disproportionately affected the North and Midlands in the UK. In the early 1990s downturn, London and the service-focused South got away lightly again compared with outlying regions.

This time, the divide has been between low-paid service sector jobs in leisure and retail and higher paid jobs which have been able to shift quickly to working from home to protect themselves. The rise in inequality implied by this has always been a feature, but the response of the political class is likely to be very different this time around. The economic orthodoxy of the 1980s and 1990s was pretty much sink or swim.
Today, the rise of populism means governments are more likely to be supportive of those hit hardest and to shun the austerity that characterised the past ten years. This will have a significant impact on many fronts, not least for inflation which is clearly not a problem in the short term.

Low levels of inflation, however, do not help erode debt through higher earnings. Mortgages, loans and personal debts will need to be managed carefully, which will impact those more in their 30's 40's and now 50's.

Fund managers and investors alike on the other hand continue to play four themes simultaneously at the moment: first, they must seek out the beneficiaries of short-term stimulus, perhaps including a reduction in consumption taxes to encourage spending; second, they may need to position themselves for another tough year in 2021, probably tougher than the market expects today; third, they need to look for the winners in a world where existing trends, to online shopping for example, and working from home, have been massively accelerated; and finally, they need to start thinking about hedges against possible inflation in the future.

One other concern for investors to keep an eye on is how governments start to think about managing their balance sheets in the wake of this year's huge stimulus. If austerity is out, then tax rises are likely to take precedence over spending cuts. An autumn budget, if not a July statement from the Chancellor Rishi Sunak, could start to indicate the direction of travel.

The good news is the latest purchasing managers' index (PMI) data for the UK shows a record recovery in June, although the economy has yet to return to growth. The *Markit* composite PMI numbers (released 23rd June) showed a reading of 47.6 for the month – a four-month high and a record jump from May's reading of just 30. Importantly, any PMI reading below 50 shows economic contraction, but the massive leap, which reflects shops and businesses re-opening, illustrates that the rate of decline has stabilised. This was the second successive month of record-breaking positive jumps in PMI numbers after they cratered to all-time lows in April. Within the composite numbers, the reading for UK services, which accounts for around 80% of the total economy, jumped to 47 in June (from 29 in May).

Meanwhile, both manufacturing and manufacturing output crept into positive territory with flash readings of 50.1 and 50.8 respectively.

Analysts expect the UK economy to return to growth in the third quarter helped by the further easing of lockdown restrictions scheduled for 4th July.

It will be too early to take any further positions in anticipation of these challenges, but we continue to gather data and will listen to the rhetoric in the meantime.

Have a good weekend, enjoy the last of the sunshine for a while.

Kindest regards

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