BROMPTON
ASSET MANAGEMENT

Quarterly review

for the three months to 30 June 2020

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Global equities rose 19.81% in sterling over the second quarter of 2020, more than regaining the previous quarter's loss to stand 0.80% higher than at the start of the year. Investor confidence returned following the swift action of central banks and governments to mitigate the economic impact of the Covid-19 lockdowns on businesses and households through large-scale monetary and fiscal support. Global bonds rose 3.68% in sterling.

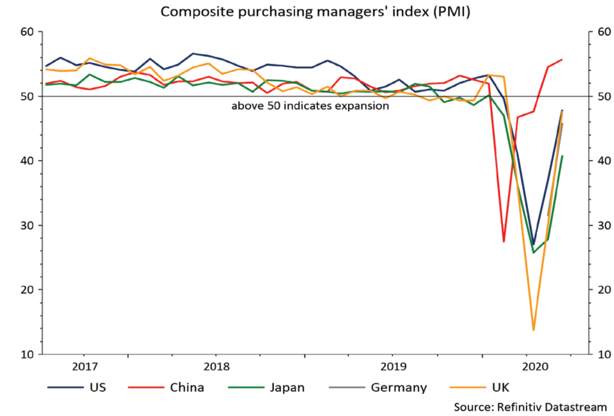
Monetary easing is likely to remain in place for some time. In June, a majority of Federal Open Market Committee members forecast that US official interest rates would remain near zero until the end of 2022. In the same month, the Bank of England announced further quantitative easing of £100 billion in addition to the £200 billion announced in March while the European Central Bank increased its asset purchase programme from €600 billion to €1,350 billion.

Commentators were divided on the longer-term impact of so much monetary and fiscal easing on inflation. The measures adopted at the time of the 2007-09 global financial crisis may not have proved inflationary because capital was required to rebuild bank balance sheets. A generally stronger banking sector may on this occasion result in a much greater impact on the economy from these extraordinary measures and ultimately fuel inflation.

The widespread relaxation of lockdown restrictions added to the optimism as the numbers of new cases of Covid-19 in Europe declined although the rising trend in the US was a concern. Positive news on the early-stage quest for vaccines and treatments also aided the market recovery although a widely-available medical solution appeared a distant prospect.

Key leading indicators such as the purchasing managers' indices (PMIs) rose sharply over the quarter as the chart opposite shows and may imply a faster-than-anticipated economic recovery. China's composite PMI rose to 54.2 in June; a PMI above 50 suggests that economic expansion is on the horizon. In the eurozone, the UK and the US, where lockdowns were imposed later, PMIs in June were recovering but still stood below 50.

Jobs data, typically regarded as a lagging indicator, also surprised positively. In May and June, the numbers in employment in the US rose by 2.5 million and 4.8



million respectively, albeit from a low base following the 20.5 million jobs lost in April. US unemployment fell from a post-lockdown high of 14.7% in April to 11.1% in June. Eurozone unemployment rose from 7.3% in April to 7.4% in May, the latest date for which this data is available. In the UK, unemployment increased from 3.8% in March to 3.9% in April but the worst may be yet to come as furloughed workers and 425,000 "inactive" workers were excluded from the number of unemployed. Joblessness looks set to rise as the government's furlough scheme is wound down.

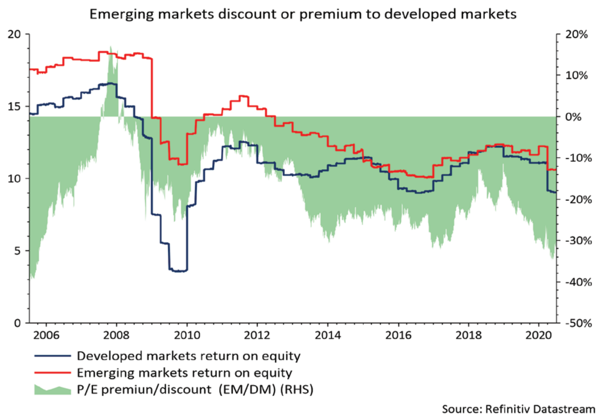
US equities outperformed over the quarter, rising 20.97% in sterling, with technology stocks particularly strong, up 32.33%. Technology stocks were benefiting from an acceleration in established trends towards more home working and online shopping and entertainment. US equities, however, may prove vulnerable to the resurgence in Covid-19 cases and increased political risk because the Democratic presidential candidate, Joe Biden, who is likely to favour increased corporate taxes, has led in the opinion polls covering voters' intentions in November's election.

Equities in Asia excluding Japan and emerging markets rose 17.20% and 18.60% respectively in sterling as Covid-19 numbers were successfully contained for now and the Chinese economy rebounded strongly from lockdown. Sino-US tensions resurfaced, however, after China passed a new security law governing Hong Kong. Emerging market equities ended the quarter lowly valued relative to some developed economy stockmarkets, as the chart below shows, and this may provide a buying opportunity. The growing representation of faster-growing technology stocks in some emerging markets adds to

Quarterly review (continued)

for the three months to 30 June 2020

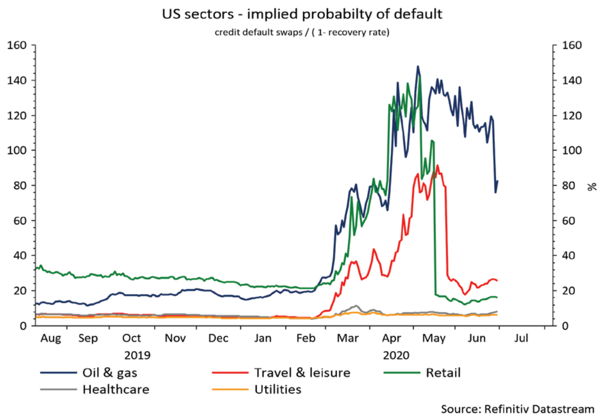
the attractions of generally lower public sector debt and higher potential economic growth rates compared to some developed economy peers. The liquidity measures adopted by the Federal Reserve may also lead to dollar-weakness and foster capital flows into emerging markets.



Equities in Europe excluding the UK rose 18.49% in sterling as the European Commission's €750 billion recovery plan took shape, with German stocks particularly strong, up 27.28% in response to Berlin's €130 billion stimulus package.

UK stocks lagged, however, rising only 8.17% as investors continued to favour growth companies over more cyclical value companies in the energy, industrial and financial sectors, which account for a significant proportion of the UK stockmarket. Dividend payments from UK companies are also expected to fall more severely than dividend payments from US and eurozone companies. Continued uncertainty surrounding European Union-UK trade negotiations, which passed the 30 June deadline for extending the Brexit transition period, also proved a headwind for UK stocks. UK smaller companies, however, outperformed, gaining 16.60%.

UK government bonds returned 2.58% but sterling corporate and high yield bonds did better, returning 9.03% and 10.71% respectively as central bank and government support for companies led to a reduced risk of default, particularly for the badly affected retail and travel and leisure sectors, as the chart below shows.



Liquidity improved in corporate bond markets as the Fed effectively extended the scope of its asset purchase programme to include some investment grade corporate bonds. Emerging market debt returned 11.60% in sterling as emerging market central banks cut interest rates in response to the crisis. Gold and gold equities rose 12.46% and 54.10% respectively in sterling over the quarter as near-zero interest rates reduced the opportunity cost of holding this nil-yielding asset.

I remain positive overall on the outlook for equities despite the remarkable recovery over the quarter because of the largescale policy support from central banks and governments. In an environment of near-zero interest rates, investors may be justified in according higher valuations to companies capable of growing profits and dividends. Corporate bonds may also perform well as yield spreads over sovereign bonds narrow. An allocation to gold and gold equities may provide diversification and potentially some capital protection.

Important information

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