BROMPTON ASSET MANAGEMENT

Covid-19 commentary

16 April 2021

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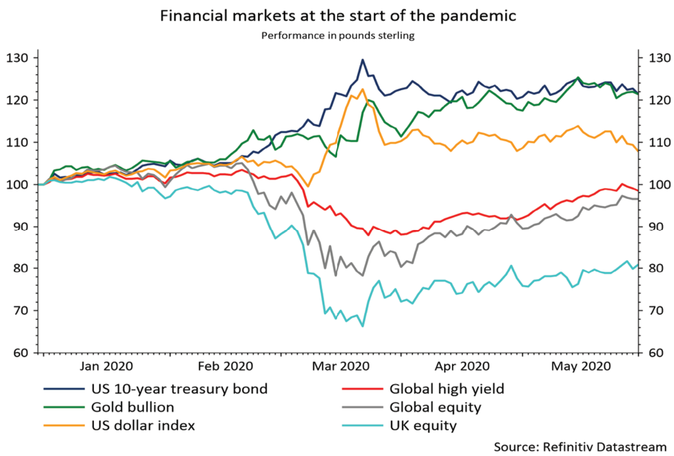
Lessons to learn from a tumultuous year in markets

A little more than a year ago, the rapid spread of Covid-19 beyond its epicentre in the Chinese city of Wuhan forced governments around the world to announce lockdowns and led to a partial shut-down of the global economy. In the UK, Boris Johnson, the prime minister, ordered an end to non-essential contact and travel on 16 March 2020 and announced a full lockdown seven days later. It is worth reflecting on market reactions to this historically-significant public health crisis and examining the opportunities for investors today.

The benefit of diversification

Global equities fell 25.33% in sterling terms from their peak on 20 February 2020 to their 16 March low point. Over the same period, some risky assets fell more than global equities.



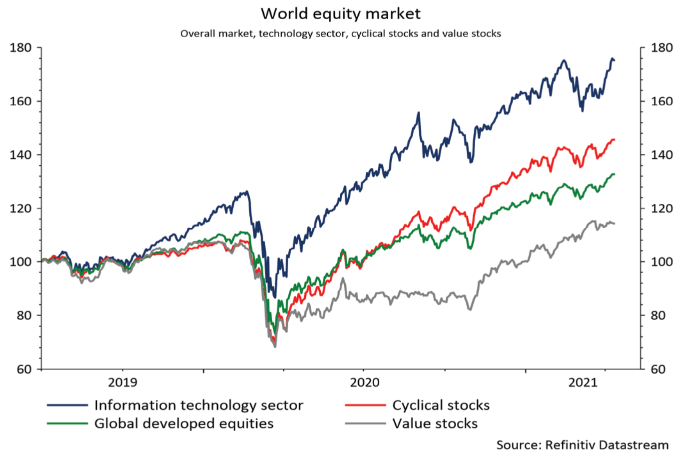
- UK equities overall fell 30.28% while smaller stocks fell 37.14% because of the London market's heavy weightings in cyclical sectors such as energy, financial services and industrials. Futures markets implied that UK dividends would decline more steeply than dividends in the US and Europe excluding the UK.
- Sterling corporate investment grade and high-yield bonds fell 7.31% and 10.41% respectively as default risk rose.
- Oil prices fell 44.10% in sterling as the demand shock coincided with the price war between Russia and Saudi Arabia.

Safe-haven assets, however, made gains.

- Global bonds returned 5.46% in sterling while UK government bonds gained 1.30%.
- The dollar and yen gained 4.91% and 11.30% respectively against sterling.

The divergence in performance between risky and defensive assets demonstrates the importance of diversification across different asset classes. Brompton's multi-asset strategies showed smaller declines over the period as investments in cash, bond holdings and defensive alternative holdings lessened the impact of the falls by equities and other risky assets.

Rewards for longer-term investors



As the chart above shows, long-term investors who stayed the course when markets fell have been rewarded. Exceptional monetary and fiscal support from the world's leading central banks and governments cushioned the impact of the lockdowns for businesses and households and restored confidence.

Global equities rapidly recovered to pre-pandemic levels and went on to post a 49.46% gain in sterling between their 16 March 2020 low point and 31 March 2021.

Over the same period, other risky assets also recovered.

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- US technology stocks rose 73.20% in sterling as lockdowns accelerated the adoption of new technologies.
- Economically-sensistive UK smaller companies rose 72.18% as the UK's trade deal with the European Union dispelled fears of a hard Brexit and rising vaccinations promised a return to normality.
- Sterling corporate and high-yield bonds returned 8.99% and 17.16% respectively as the risk of default diminished and liquidity increased and the Federal Reserve bought corporate bonds for the first time as part of its quantitative easing programme.

Conversely, defensive assets fell.

- Global bonds and UK government bonds fell 7.83% and 3.88% in sterling.
- The dollar and yen fell 11.02% and 14.92% respectively against the pound.

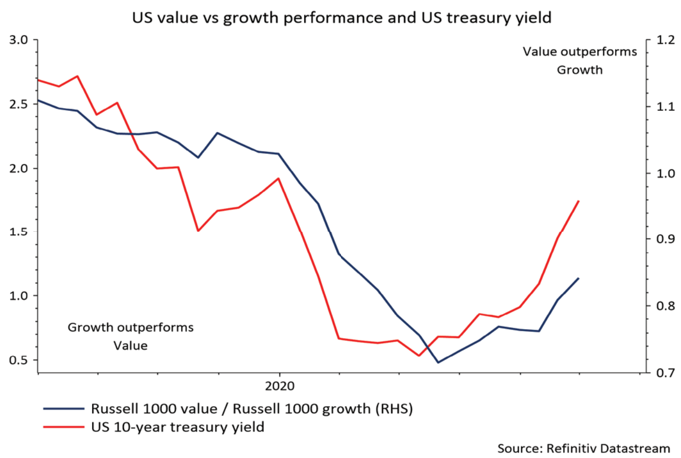
During this period, the Brompton multi-asset strategies outperformed their respective benchmarks.

Opportunities for active managers

The Brompton multi-asset strategies benefited from active management as the falls for some risky assets provided good buying opportunities and the fund management team added to the allocations to equity and credit. Panic-selling also provided opportunities in some strategies to add to the 3i Infrastructure investment trust, which fell to a wide discount to its net asset value; similar conditions provided an attractive entry point for purchases of the TR Property investment trust in some strategies.

Looking ahead

In late 2020, good news on vaccines led to a rotation in equity market leadership from growth stocks to cyclical and value stocks. Inflation expectations and longer-dated bond yields rose because of stronger oil and commodity prices, pent-up consumer demand and supply-chain disruption.



Moderate inflation is tyically good news for equities and the investment team remains positive overall although the team has increased investment in holdings managed in accordance with a value style of investing. Within the strategy's bond allocations, a bias towards shorter-dated and inflation-linked bonds should provide some protection from a further rise in bond yields. Gold and gold equities provide diversification and may perform well should inflation remain above interest rates.

Important information

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