



## WHAT A RIDE IT HAS BEEN!

January 2021

Equities worldwide fell over 30% in eight weeks from 20th January to 23rd March, yet by the end of 2020 markets had recovered all this fall and, in some cases, finished the year higher than they started. Our overview this month explores the catalysts that made 2020 such an extraordinary year for investors, whilst we also consider the risks and opportunities that may influence returns in 2021.

Timeline of major events throughout 2020:

<b>Jan 3rd</b>	US Drone strike kills top Iranian Security General in Baghdad, Iraq	<b>Apr 3rd</b>	London's Nightingale hospital opened - 4,000 beds ready to help treat patients
<b>Jan 15th</b>	US and China sign "Phase one" trade deal	<b>Apr 5th</b>	Boris Johnson admitted to hospital suffering with Covid
<b>Jan 16th</b>	Impeachment trial of US President Donald Trump begins	<b>Apr 6th</b>	Japan announce state of emergency and \$1tn in stimulus
<b>Jan 22nd</b>	China locks down the city of Wuhan as death toll rises	<b>Apr 20th</b>	Price of oil turns negative for the first time in history
<b>Jan 26th</b>	Basketball legend Kobe Bryant dies in a helicopter crash	<b>Apr 23rd</b>	Donald Trump suggests coronavirus could be treated by injecting disinfectant
<b>Jan 29th</b>	Covid cases in China surpass those of SARS	<b>Apr 28th</b>	US Death toll of 58,365 surpasses that of US soldiers killed in Vietnam war
<b>Jan 30th</b>	WHO declares Coronavirus a Public Health Emergency	<b>May 7th</b>	US unemployment claims hit 33.3m or 20% of workforce vs two months prior
<b>Jan 31st</b>	United Kingdom formally withdraws from the European Union	<b>May 10th</b>	Global cases hit 10m
<b>Feb 5th</b>	US Senate votes to acquit President Trump on charges of abuse of power	<b>May 25th</b>	George Floyd is killed during arrest, prompting global protests
<b>Feb 23rd</b>	First European Covid outbreak in Italy. 10 towns in Lombardy locked down	<b>Jun 1st</b>	Donald Trump threatens military force to quell protests over death of George Floyd
<b>Feb 27th</b>	Dow Jones Index suffers its biggest one day fall in history - down 1,190.95 points	<b>Jun 30th</b>	China's new national security legislation for Hong Kong comes into force
<b>Feb 29th</b>	US and Taliban sign deal to end 18-year war in Afghanistan	<b>Jul 1st</b>	Europe opens its borders to 15 safe countries
<b>Mar 6th</b>	Russia refuses to reduce oil production, breaking with OPEC. Price war ensues	<b>Jul 1st</b>	Vladimir Putin wins national referendum allowing longer presidential terms of office
<b>Mar 11th</b>	WHO declares Coronavirus a Global Pandemic	<b>Jul 4th</b>	Pubs reopen across the UK!
<b>Mar 15th</b>	Federal Reserve slashes interest rates to near zero to support economy	<b>Jul 20th</b>	UK suspends extradition treaty with Hong Kong after new Chinese security laws
<b>Mar 16th</b>	S&P plunges 12% - worst day since 1987 crash	<b>Jul 21st</b>	EU agrees huge €750bn post-Covid stimulus bill
<b>Mar 22nd</b>	India puts 1 billion people into daytime curfew	<b>Aug 4th</b>	Huge explosion at the port of Beirut, kills more than 200 and leaves 6,000 injured
<b>Mar 23rd</b>	UK enters lockdown	<b>Aug 11th</b>	Russia grants regulatory approval to Sputnik V vaccine
<b>Mar 23rd</b>	Federal Reserve pledges "unlimited" support to markets - markets rally	<b>Aug 12th</b>	UK posts worst quarterly slump on record - 20.4%
<b>Mar 24th</b>	Dow Jones jumps most in 80 years, up 2,100 points	<b>Aug 18th</b>	Joe Biden officially nominated as Democratic party candidate

<b>Mar 24th</b>	Japan postpones 2020 Olympics	<b>Aug 19th</b>	Apple becomes first company in the US to be valued at \$2tn
<b>Mar 27th</b>	Boris Johnson announces he has contracted Covid	<b>Aug 20th</b>	Russian opposition politician Alexei Navalny falls into coma after Novichok poisoning
<b>Apr 2nd</b>	Record 6.6m people file for unemployment in the prior week (10m over 2 weeks)	<b>Sep 16th</b>	Yoshihide Suga named as Japanese PM after Shinzo Abe stood down as PM
<b>Oct 2nd</b>	Donald Trump announces on Twitter he and his wife have tested positive for Covid	<b>Nov 23rd</b>	Oxford/AstraZeneca says its vaccine is up to 90% effective
<b>Oct 5th</b>	Trump leaves hospital whilst still infectious	<b>Nov 30th</b>	Biden announces Janet Yellen as US Treasury Secretary
<b>Oct 17th</b>	Jacinda Ardern re-elected in landslide NZ election	<b>Dec 2nd</b>	US Attorney General says there is no evidence of widespread voter fraud in the US election
<b>Oct 20th</b>	US Justice Department sues google for illegal monopoly over search and search advertising	<b>Dec 5th</b>	Russia Begins vaccinating citizens with Sputnik V vaccine despite not finishing trials
<b>Oct 27th</b>	A record 69.5m Americans have already voted a week before election	<b>Dec 8th</b>	UK begins vaccinations of Pfizer BioNTech
<b>Oct 30th</b>	Boris Johnson announces a second four-week lockdown	<b>Dec 11th</b>	EU agrees to cut carbon emissions by 55% in the next decade
<b>Nov 7th</b>	Joe Biden declared winner of US election	<b>Dec 12th</b>	Xi Jinping says China will reduce carbon footprint by 65% by 2030
<b>Nov 9th</b>	BioNTech and Pfizer announce their Covid vaccine is over 90% effective	<b>Dec 14th</b>	US electoral college officially vote to affirm Joe Biden as president elect
<b>Nov 13th</b>	Dominic Cummings "resigns"/is sacked by Boris Johnson	<b>Dec 18th</b>	Moderna vaccine granted emergency approval by FDA
<b>Nov 15th</b>	Trump tweets "election was rigged"	<b>Dec 25th</b>	Lapland in lockdown - Christmas cancelled
<b>Nov 16th</b>	US drug maker Moderna says its Covid vaccine is 94.5% effective	<b>Dec 30th</b>	UK MPs and EU chiefs sign and approve Brexit deal

Twelve months ago, as we entered 2020, there was significant uncertainty about the outlook for global growth, fuelled by concerns about the viability of a trade deal between the US and China. This combined with the lack of clarity about the prospects for what a post-Brexit UK would look like could easily have led investors to tread cautiously as the year began. Yet by mid-January equities had gained c2%, partly because of the relief that “Phase One” of the trade deal was signed on 15<sup>th</sup> Jan.

Up until this point, the new coronavirus that had started in a market in Wuhan in November 2019 had not caused markets any concern because it was seen as a containable risk and not much more serious than previous SARS and bird flu epidemics. That all changed when Wuhan was put into lockdown on 23<sup>rd</sup> Jan, with reports that some of its 11 million residents were welded into their apartment blocks to prevent the spread. Cynics amongst us might suggest that the Chinese delayed putting Wuhan into lockdown until after the trade deal was signed and we will probably never know whether locking down the city earlier would have helped contain the spread.

From this point until the end of March, stable and steady

markets were replaced by extreme volatility and massive swings as panic selling, the severity of which has not been seen since the 1987 Wall Street crash, hit stock-markets around the world. Daily swings in the major indices of 5% or more became common place. At the very peak of the crisis on 16<sup>th</sup> March, the S&P 500 fell 12% in one trading session, whilst the Nasdaq and Russell 2000 had their worst trading days in history and the VIX index (measure of stock market volatility) hit an all-time high of 82.69 It was the biggest daily fall in markets since the 1987 Wall Street crash and by the close of play, all of 2019’s gains had been wiped out.

From peak to the trough (23<sup>rd</sup> March), world stock-markets fell 32% in eight weeks. Whilst the coronavirus panic was the main cause, it didn’t help that Saudi had initiated an oil price war with Russia after Russia refused to cut oil production to keep prices stable. This helped fan the flames of market nervousness throughout March and contributed to oil prices falling into negative territory for the first time ever. At one point it was theoretically possible to buy a barrel of oil for minus \$38 although in reality nobody was actually paid to take physical delivery of any oil!

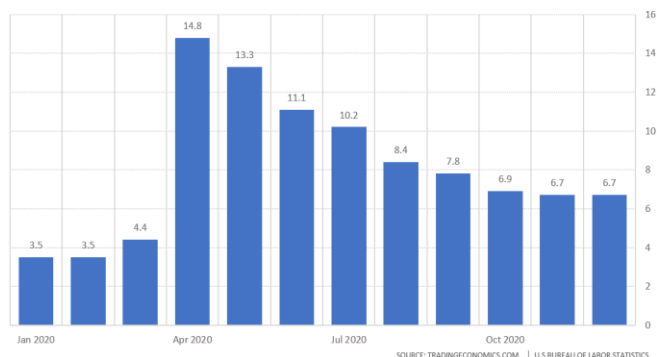
The dramatic sell-off on 16<sup>th</sup> March was attributed to the Federal Reserve cutting interest rates by 1% (to effectively 0%!) the day before. Whilst investors had been willing the Fed to act decisively ever since the coronavirus crisis began, such an extreme and unexpected rate cut was perceived as a panic move and it spooked the markets as a result.

And then, as suddenly as it had begun, the bear market was over. From 23<sup>rd</sup> March until 31<sup>st</sup> December, equity markets rose on average by 48%, to finish the year up 0.5%.

What took eight weeks to break apart took 40 weeks to put back together, and what a relief!

So, what was the catalyst for such a massive recovery, at a time when US unemployment was rising to an eventual 14.7% and GDP falling by 34.3% in the second quarter of 2020? In a word - stimulus. Massive stimulus from both central banks and governments alike. In the US, the Fed pledged an unlimited programme of bond-buying, using newly created dollars to fund it (quantitative easing). They also committed to buying \$120bn a month of corporate debt and created a Loan Facility (TALF), to support the flow of credit to consumers and businesses.

### US Unemployment (in millions)



Source: Trading Economics

What the markets really loved about this was the reference to “unlimited” support. It was a declaration that a blank cheque had just been written to support the US economy at any cost. Action from the Fed was followed by government backing too, exemplified by the US passing a \$2trn support package. This, amongst other measures, gave each eligible adult a payment of \$1200, created a \$500bn loan pool for businesses, states and municipalities and a \$350bn package of loans to small businesses to cover salaries and other expenses.

The UK, Europe and other major economies’ central banks and governments followed suit with similar packages of measures – we won’t go into detail, but you get the general

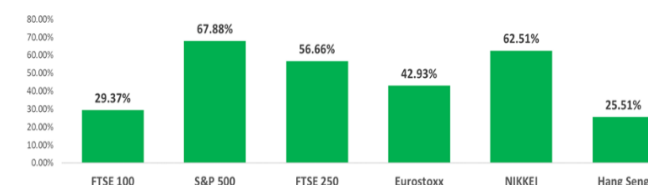
idea that there was a massive, coordinated and aggressive policy response to the crisis, and it all came at around the same time, resulting in global markets recovering most of what had been lost, and in some cases gaining ground over the year.

Whilst the sell-off was indiscriminate and affected most markets fairly equally (UK, US, Europe and Japan all fell c30% or more), the huge rally after 23<sup>rd</sup> March affected markets very differently:

1st Jan to 23rd March 2020 - most markets fell in-line with each other...

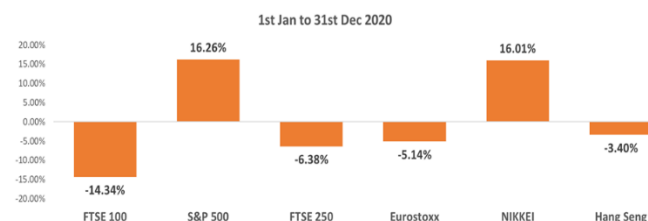


...but not all markets went up in-line with each other afterwards - 23rd Mar to 31st Dec 2020



Source: Morningstar

This created a large disparity in returns over the 12-month period. For instance, the US and Japanese markets both ended the year up 16%, whereas the FTSE 100 finished the year down 15%! See below:



Source: Morningstar

So why was there such a big difference between the best and worst performing countries’ stock-markets over the year? It all comes down to sectors.

During the coronavirus pandemic, the businesses most impacted have been traditional companies in sectors such as retail, hospitality, travel and leisure that rely on physical footfall and positive economic conditions to thrive. Conversely, technology companies have soared as consumers and businesses worldwide have been forced to stay at home and consume more of their services (Zoom is the perfect example!). The combined sales of Amazon,

Alphabet, Facebook and Apple rose 18% year-on-year to October, and their combined profits jumped 31% to \$39bn. These four companies make up 18% of the US S&P 500 and technology stocks in general account for 28% of the index. On the other hand, the FTSE 100 is generally comprised of those traditional sectors that have been impacted by coronavirus, and our domestic index has only 1.37% exposure to technology companies. Therefore, the US stock-market has performed well over the year, whilst the FTSE 100 has fallen. Similar trends emerged amongst the other world stock-markets, with tech providing positive momentum, but counterbalanced by negative momentum from traditional sectors.

It is easy to forget that there have been some other very important themes that have developed in 2020 but have been overshadowed until recently by coronavirus.

We've mentioned the trade war and oil price war already, but other factors such as political unrest in Hong Kong, last minute Brexit wrangling, Trump's impeachment, the Black Lives Matter movement and of course the US election have all had major influence this year. Would Joe Biden have won if it were not for the increasing weight of public opinion against Trump's handling of US anti-racist protestors? It is impossible to say but coronavirus certainly did shift the election in Biden's favour, playing a very important role in pushing some of the 25 million unemployed American voters into the waiting arms of the Democrats.

When Biden was announced as the 46<sup>th</sup> US president (elect), despite the protestations from the Trump team, markets pushed higher after a wobbly preceding month, debunking the supposition that Republicans are good news for equities. Shortly afterwards on November 9<sup>th</sup> Pfizer announced that their vaccine was effective and ready to go (did they finesse the timing of that announcement by waiting until after the election?!) and the markets were off to the races again!

The various vaccines that have already been announced and approved were the real game changer in 2020. Evidently there was significant capital waiting on the side lines for vaccines to be approved because when the Pfizer vaccine was announced, there was a structural shift in markets. For more than three years, 'growth' has outperformed 'value'. In other words, companies that are expensive today based on their earnings but promise the chance of much greater earnings in the future have been favoured over traditional, steady businesses that rely on a favourable economy. We wrote about it in July 2020 and have mentioned the 'growth versus value' debate many

times before. With Pfizer's announcement, there started an immediate shift back into 'value' stocks and away from 'growth'. European banks, global energy and airlines all soared more than 30% in November and small US companies performed twice as well as the S&P 500. Whilst too early to call a complete rotation to towards these unloved sectors, the vaccines have provided markets with confidence that a structural recovery in the global economy may be coming, and this was enough to start the ball rolling.

They left it to the last minute, but the recently signed Brexit deal, irrelevant of whether it is a good deal or not, in conjunction with this value rotation has proven to be a short-term catalyst for strong relative UK equity market performance. Aside from a two-week period post the election last year, the UK equity market has been much maligned for several years and fund flows into the UK over the coming months will provide a good indication of whether international investors are once again considering the UK for a proportion of their equity allocation. In the first week of 2021 the FTSE 100 and FTSE 250 have been the strongest of all the major indices, with the FTSE 100 rising by 5.90% in the first three trading sessions.

But what does the rest of 2021 have to offer? Some seasoned commentators are becoming concerned about the valuation of equities and have predicted that this is a bubble that will burst sooner rather than later. Last year, expensive companies became even more expensive and there is concern that at some point the music must stop. Tesla was the stock-market darling of 2020, rising over 700% during the year, propelling Elon Musk's car maker into the S&P 500 as the 5<sup>th</sup> biggest company in the index, with a market capitalisation of \$700bn. As a result, Elon Musk has overtaken Jeff Bezos of Amazon as the world's richest person. Yet Tesla's market valuation is over \$1.5 million per car sold each year versus \$9,000 per car for GM. Either Tesla has to grow exponentially, or its share price has to fall but try telling that to the short-sellers who lost \$38bn last year betting that Tesla's share price would fall!

There are some major questions that we feel will determine the outcome for markets in 2021.

1) Will the vaccines do their job and set the global economy back on the path to growth? Watch out this year for the term "vaccine escape" – the term used to describe how viruses evolve to render vaccines ineffective. Sadly, this might be a term that the world becomes very familiar with in 2021. Thankfully, like the annual flu jab, apparently tweaking existing vaccines to counter mutant viruses is fairly straight-forward, albeit costly and time consuming.

2) What does a Biden/Harris White House with a Senate and Congress majority mean for business? Early signs are positive for 'value' but 'growth' sectors like tech have been jittery. Biden/Harris won't have it all their own way due to some centre-leaning Democrat Senators who will veto certain policies but expect more left-leaning policies to be implemented.

3) When will interest rates start to rise? The Fed has pledged to stoke inflation before hiking rates but to think that rates won't rise for a decade is delusional. We believe that there could be no move in interest rates for at least 6 months and possibly much longer but expect market volatility when they do start to rise.

### **GOODBYE DONALD!**

We have all heard enough about it, but unfortunately coronavirus remains the key theme as we progress through 2021. Warren Buffet is bullish - he described the US

economy as a train that had not been derailed by coronavirus but that had been taken off the tracks and put in the sidings for safe-keeping. Once the crisis is over the train will continue on its path, the key point being that the track isn't broken, and the engine still runs.

We are confident the global economy will overcome the pandemic this year and still feel that equities offer the best opportunity for growth, assuming that vaccines do their job and that Biden takes a measured approach to change. Whether this proves to be the start of the great rotation out of 'growth' and into 'value' remains to be seen but there is certainly a good argument to suggest that this shift has already started.

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