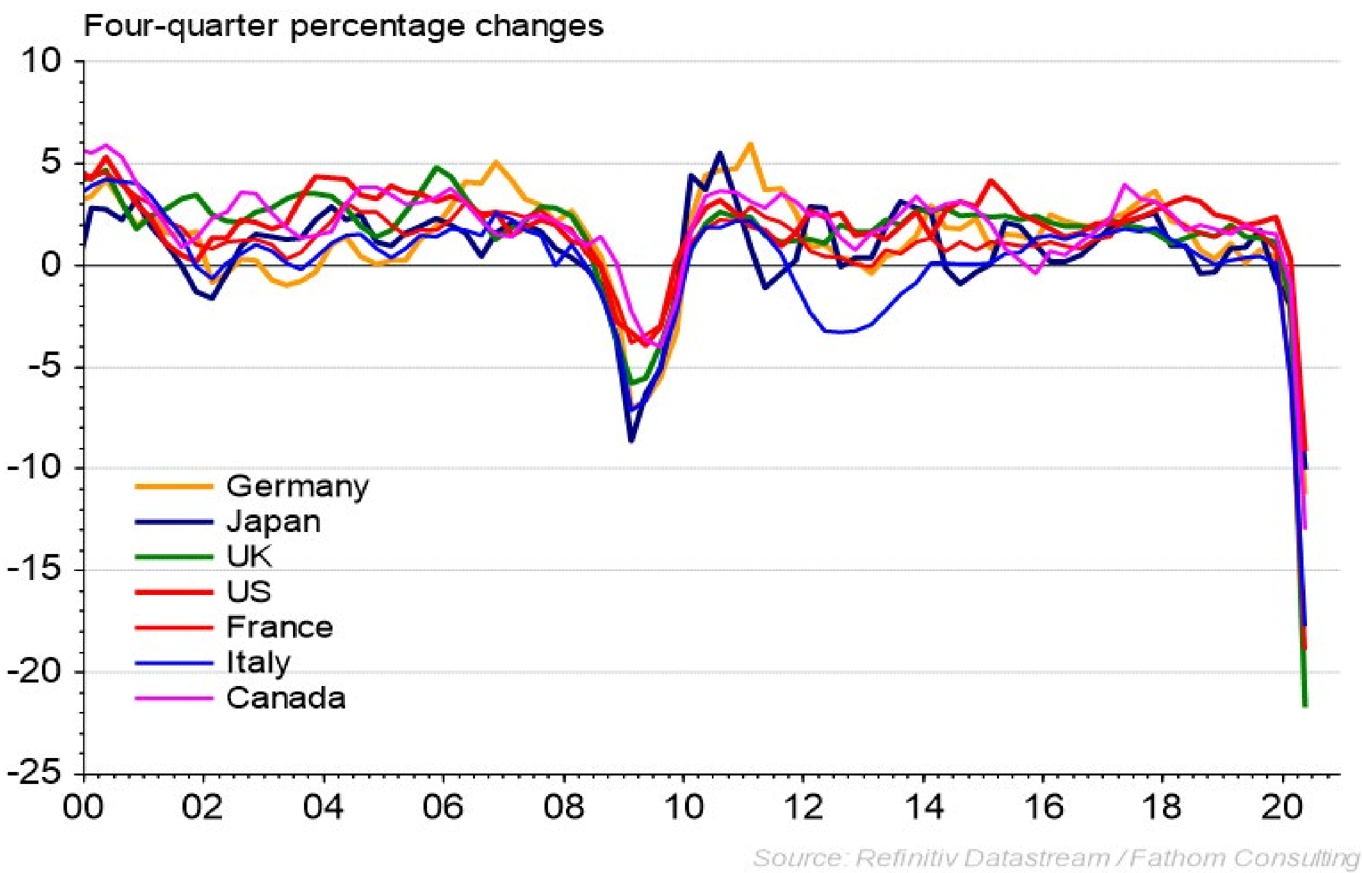
Recent economic developments

■ Data released over the past month showed that the global economy continues to recover from the sharp contractions in activity recorded in the second quarter of 2020. In the US, key indicators of economic activity show ongoing improvement but the pace of activity has slowed from the initial burst seen in the first couple of months following the reopening of the economy.

■ In the US labour market, which took a severe hit from the lockdown, data showed that employers continued to bring back furloughed workers in August, albeit at a slower pace than in the previous two months. Overall, the US economy added 1.4 million jobs in August (versus 1.7 million jobs and 4.8 million jobs added in July and June respectively). Payrolls are still more than 11 million jobs below the pre-pandemic level. The unemployment rate fell to 8.4%, down from the covid-19 recession peak of 14.7% recorded in April 2020.

■ In the UK, the Office for National Statistics (ONS) confirmed that gross domestic product (GDP) fell in the second quarter by 20.4% compared with the previous three months. That marked the biggest quarterly decline since comparable records began in 1955. The data also showed that the UK economy underperformed all other G7 economies in the second quarter of 2020 (as shown in Figure 1). However, in line with other major developed economies, the UK economy has staged a recovery since the latter part of Q2. For instance, according to the ONS, following a record contraction in April, monthly GDP grew by 2.4%, 8.7% and 6.6% in May, June and July respectively as lockdown measures eased.

Figure 1: G7 GDP growth rate



- In the equity markets, a gain of 7.1% in August pushed the US benchmark S&P 500 index to record highs. Technology stocks led the gains for the month, with the Nasdaq Composite index adding 9.7% in total return for the month. Outside the US, Japan's Nikkei 225 rose by 6.6% in August. Germany's DAX gained over 5.1% and the UK's FTSE 100 index returned 1.75% for the month (all local currency, total returns). For the year-to-date as at the end of August, the US S&P 500 index had returned 9.6% and the Nasdaq Composite had returned 31.3%. In contrast, , Japan's Nikkei 225, Germany's DAX and the UK's FTSE 100 index had delivered local currency total returns of -1.27%, -2.3% and -18.9% respectively.

- Increased risk appetite meant that fixed income markets had a poor month in August as investors rotated into riskier assets. Government bond yields rose (and capital values declined) across the US, UK and Germany. Confirming the rise in risk appetite, high yield bonds outperformed investment grade credit during the month. In the foreign exchange markets, the US Dollar (USD) fell to a 2-year low in August as it declined for the 5th consecutive month. The USD's weakness meant that the euro strengthened above $1.19 for the first time in over 2 years. Sterling also rose against the USD. However, the ongoing uncertainty surrounding the Brexit trade negotiations should weigh on sterling in the weeks ahead.

- Looking ahead, while there will be periodic bouts of elevated volatility, our base case expectation is that in the absence of renewed lockdowns or fiscal policy errors that stifle the nascent recovery, the prevailing backdrop of extensive monetary stimuli, particularly in the US, should continue to support financial markets in the months ahead.

- Consequently, we continue to position portfolios in line with longer term strategic asset allocation positions, balancing the desire to participate in broad market gains with the ongoing need for downside protection.

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