Recent economic developments

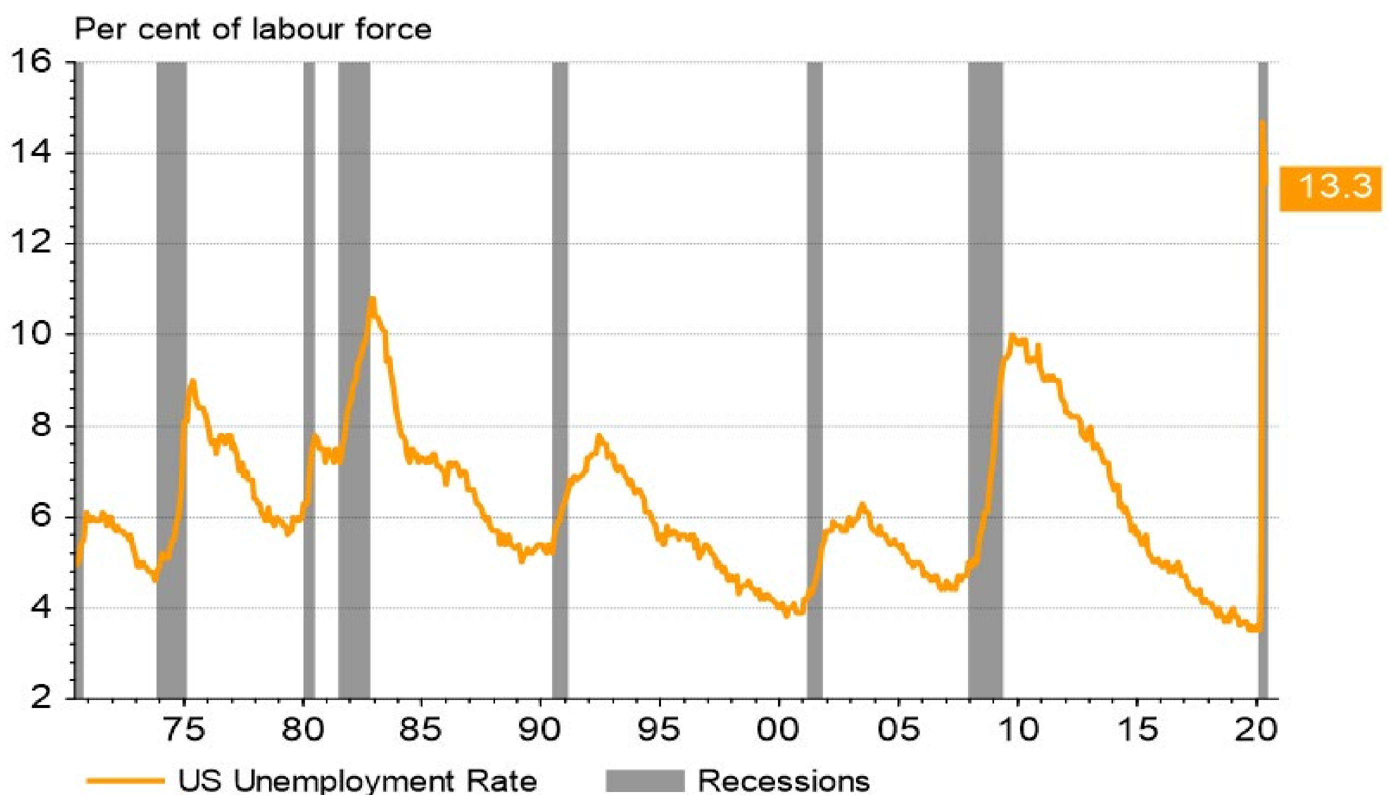
■ Following the pandemic-induced contractions in economic activity over the past few months, recent steps to reopen economies have resulted in a rebound in economic data across the major developed markets. In the US, the most prominent example of this was seen in the labour market where 2.5 million people were hired in May. That marked the biggest gain in nonfarm payrolls on record. The job gains resulted in a drop in the headline unemployment rate to 13.3% from 14.7% in April.

■ While the better-than-expected labour market data has fuelled optimism about the potential economic recovery, it is important to note that even if unrevised, the strong performance in May merely marks the start of what is likely to be a long and drawn out recovery in the unemployment rate to get back to its pre-Covid-19 level.

■ In Europe, the severity of the decline in economic activity is helping to focus minds across the region and plans for further substantial fiscal stimulus are ongoing. Also, following its recent meeting, the European Central Bank (ECB) increased its bond-purchasing program by EUR600 billion and extended the scheme's duration to June 2021 – or until it believes the crisis is over. The central bank maintained interest rates at current levels as it downgraded its economic projections for the region.

■ Similarly, in its most recent monetary policy report published in May, the Bank of England (BoE) downgraded its outlook for the UK economy and flagged the risk that the coronavirus crisis could push the economy into its deepest recession in 300 years. The BoE estimates that the economy could shrink by 14% in 2020, marking the largest fall since 1709.

Figure 1: US Unemployment Rate



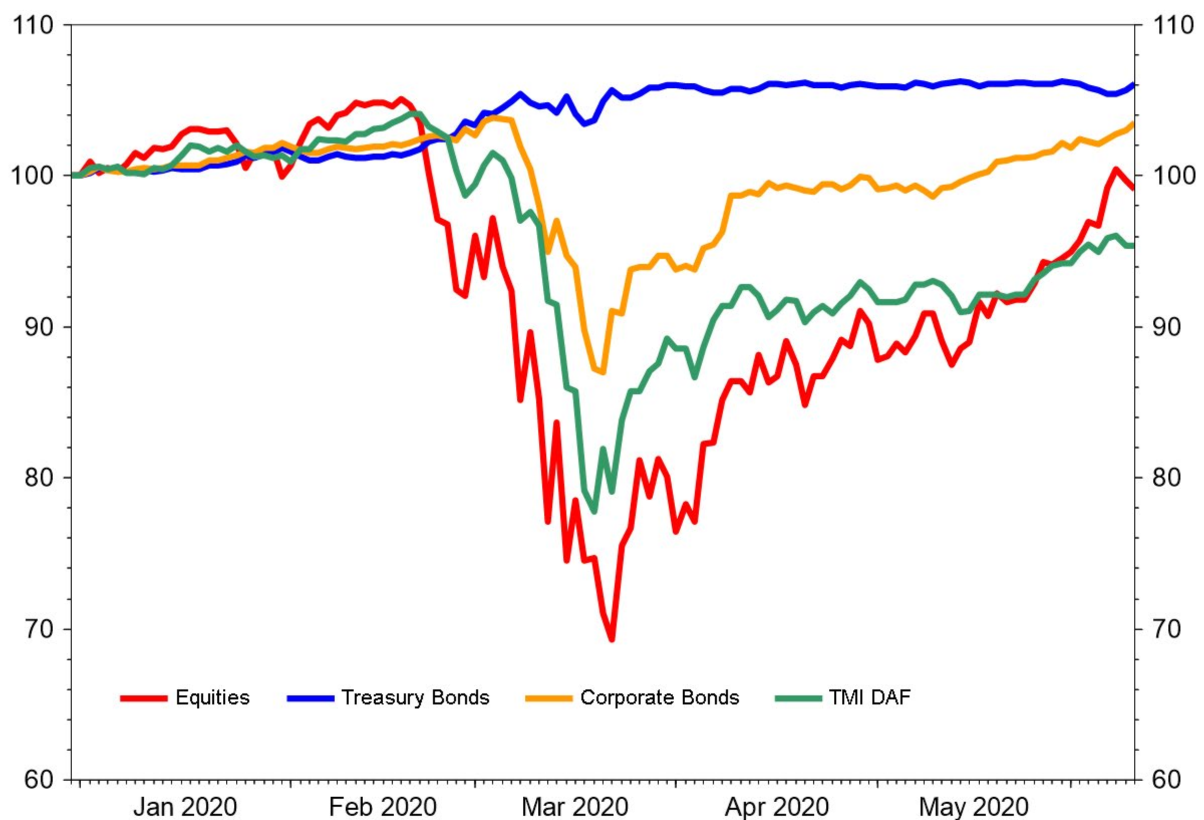
■ The nature of the economic contraction, characterised by sudden stops in economic activity, triggered by lockdowns designed to contain the pandemic means that once economies re-open, we should see positive spikes in activity, driven by a release of pent-up demand. Therefore, as economies re-open, it might be tempting to view the initial flurry of activity as evidence of a much-hoped-for V-shaped recovery. However, the weight of evidence suggests that the path to pre-pandemic levels of economic activity is likely to be protracted.

Financial markets & investment strategy

■ The rally in risk assets that began in late March persisted through May as investors were encouraged by steps taken to kick start economies across the globe. News of progress on the development of potential coronavirus treatments also supported risk appetite.

■ In equity markets, there was some sector rotation in May as technology stocks, which had led the initial stages of the rally, lagged cyclical sectors. Within fixed income markets, corporate bonds continued to benefit from strong support from the US Federal Reserve but performance was skewed towards high yield bonds. Again, this marked a notable rotation as high yield bonds had lagged their investment grade counterparts during the initial phase of the rally. In other markets, the US dollar suffered

Figure 2: 2020 year-to-date performance of selected assets



Source: Refinitiv Datastream

Note: Figure 2 shows equities (S&P 500 ETF), government bonds (3-7yr US Treasury ETF), corporate bonds (Intermediate-Term Corporate Bond ETF) & alternatives (TMI Diversified Assets Fund).

a broad decline, in line with the improvement in investor sentiment while commodities rallied, with crude oil in particular recording sharp gains (e.g. the price of West Texas Intermediate Crude closed the month up 88%). Finally, alternative assets recovered further in May, with listed property, infrastructure and private equity all posting monthly gains. Figure 2 illustrates the ongoing recovery in a range of assets that can be viewed as proxies for the components of a balanced portfolio.

- In our view, the strength of the rally in risk assets from late March belies the ongoing elevated level of uncertainty surrounding the outlook for the global economy and financial markets in the months ahead. For this reason, we retain a cautious approach to asset allocation, balancing the need for downside protection with the desire to participate in broad market gains.

- Overall, our assessment of the balance of risks means that we continue to position client portfolios close to benchmark levels across the major asset classes.

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