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INVESTOR

Economic & Political Roundup

Monthly roundup | Investment companies | September 2020

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A collation of recent insights on markets and economies taken from the comments made by chairmen and investment managers of investment companies – have a read and make your own minds up. Please remember that nothing in this note is designed to encourage you to buy or sell any of the companies mentioned.

Exchange rate	31/08/20	Change on month %
GBP / USD	1.3085	+2.2
USD / EUR	0.849	(1.3)
USD / JPY	105.83	+0.1
USD / CHF	0.9129	(1.0)
USD / CNY	6.9752	(1.8)

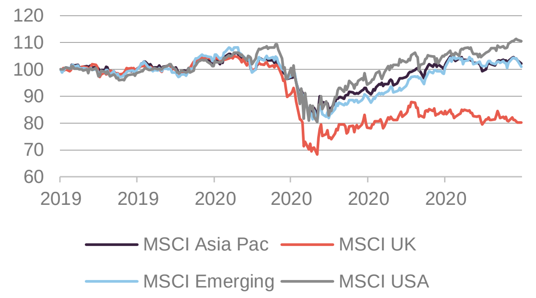
Source: Bloomberg, Marten & Co

Roundup

The S&P 500 had its best August in 34 years in what very a much risk-on end to the summer. Gold's rally took a breather while 10-year government bond yields in the UK and US were up sharply (pushing bond prices down) as technology continued to propel the post-March recovery in markets.

MSCI Indices rebased to 100

Time period 01/09/2019 to 31/08/2020



Source: Bloomberg, Marten & Co

	31/08/20	Change on month %
Oil (Brent)	45.28	+4.6
Gold	1967.8	(0.4)
US Tsy 10 yr yield	0.7048	+33.4
UK Gilt 10 yr yield	0.311	+199.0
Bund 10 yr yield	-0.398	(24.2)

Source: Bloomberg, Marten & Co

Global

COVID 'winners' leaving 'losers' behind

Teddy Tulloch, chairman of EP Global Opportunities, says it is difficult to gauge the strength of the recovery with unemployment likely to increase for a while and further corporate bankruptcies seen as inevitable. He adds that while it is expected that any faltering in the recovery will be met with further stimulative measures, governments have already significantly increased their budget deficits.

Murray International's manager, Bruce Stout, provides a region-by-region overview of the current state of affairs. The expectation is for every major economy to contract, against a backdrop of lower growth, record low bond yields and companies struggling to achieve meaningful earnings growth, in the short term.

Witan's chairman, Andrew Ross, discusses the extreme performance differential between the 'COVID winners' and 'COVID losers,' since March. He says that those that recall the dotcom boom in 1999 know well that stocks can get ahead of themselves, even when the subsequent achievements of technology outstripped assumptions made at the time.

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BY MARTEN & CO

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Allianz Global Investors

August highlights

In addition to the global funds, this month's highlights include:

Flexible investment

Inflation to remain subdued or even negative over the next year

Peter Hewitt, the manager of BMO Managed Portfolio Growth, believes that that inflation will remain subdued, or even move close to negative over the next year and interest rates in the UK, Europe and the US will also remain at extremely low levels. He adds that the case for exposure to sectors which offer secular growth characteristics remains in place. When inflation and interest rates are low and growth scarce then investment companies focussed on sectors such as technology, healthcare and biotechnology are likely to continue to prosper.

It has been very challenging valuing many illiquid asset classes

Henderson Alternative Strategies's chairman, Richard Gubbins, says that for many illiquid asset classes, net asset values for the first quarter will not be available for some time and the full financial impact will take time to become clear. The consequence of such limited visibility is reflected in wider spreads for many assets.

The manager of RIT Capital Partners believes that even if very low-interest rates make equities the 'only show in town' for some investors, a significant amount of good news is already priced in.

UK

Second-quarter reporting by companies will dictate the next leg of credit market reaction

Acorn Income's managers, Chun Lee and Robin Willis note that financial markets have been predominately focussed on the benefits of massive stimulus and less so on the risk to growth from the fallout of the pandemic. In their view, the second-quarter reporting season could therefore lead to a further weakening of credit metrics leading to more downgrades from credit rating agencies.

William Meadon and Callum Abbot, managers of JPMorgan Claverhouse, reflect on the fact that going forward, much rests on what kind of economic and earnings recovery arrives in the post-pandemic world and whether stimulus packages can offset the damage inflicted by shutdowns. The sheer magnitude of central bankers' intervention suggests they are extremely concerned about long term economic scarring. They clearly worry that lingering economic weakness may soon become a problem for all.

The UK's prospect appear particularly unclear, with uncertainty over Brexit lingering

The manager of Aberforth Smaller Companies believes that the prospects for the UK seem particularly unclear. This is reflected in sterling's leadership in the foreign exchange unpopularity contest, with 7% drops against both the dollar and the euro in the first half. Several of the attributes that have made the UK an attractive economy in which to invest seem under threat. Dividends have been slashed, pre-emption limits have been relaxed, the government has greater influence on the corporate sector and rules are being set informally without clear legislation. The manager says that as temporary adjustments to cope with the impact of COVID-19, these are understandable, though a greater role for fiscal spending was likely even before the onset of the virus. The concern is that they herald more lasting changes at a time when the UK's future relationship with Europe and the future openness of its economy are moot.

Global emerging markets

The manager of Ashmore Global Opportunities discusses why most emerging markets have been coping relatively well through the pandemic.

Many emerging markets have been less affected by the pandemic

Michael O'Brien, the manager of Fundsmith Emerging Equities, believes that in terms of structural change, the three biggest impacts will be formalisation, digitalisation and consolidation. It is also noted that the economic impact of COVID-19 on emerging markets is lower than that in the developed world, with most emerging markets are also forecast to revert to growth close to their long-term rate next year.

Hedge funds

The stock market rally has been distorting the reality on the ground for most businesses in the US

In explaining the stock markets resurgence, Bill Ackman, manager of Pershing Square, says that we have a corporate inequality phenomenon in addition to an income inequality problem. He says that if there were a stock market index of private, small businesses, it would likely be down 50% or more.

The manager of the BH Global and BH Macro funds, says that so long as a V-shaped recovery in risky assets fails to create a V-shaped recovery in economic activity, this tension is a recipe for increased volatility.

Other

We have also included comments on North America from JPMorgan US Smaller Companies and JPMorgan American; Europe from European Assets and Fidelity European Values; Asia Pacific from Aberdeen Asian Income; Japan from Fidelity Japan; India from Aberdeen New India; debt from City Merchants High Yield, Axiom European Financial Debt, and Riverstone Credit Opportunities Income; private equity from Apax Global Alpha, BMO Private Equity, Princess Private Equity, Pantheon International, and LMS Capital; technology & media from Allianz Technology; infrastructure from BBGI SICAV and Premier Global Infrastructure; renewables from Renewables Infrastructure; the environmental sector from Impax Environmental Markets; commodities & natural resources from BlackRock World Mining and Riverstone Energy; UK property from Empiric Student Property, Impact Healthcare REIT. Tritax Big Box, and UK Commercial Property REIT; and Irish property from Yew Grove REIT.

Global

(compare global funds **here**)

Teddy Tulloch, chairman of EP Global Opportunities – 20 August:

There are clear signs of an economic recovery as the "lockdown", imposed to limit the spread of the virus, is eased. It is difficult to gauge the strength of the recovery with unemployment likely to increase for a while and further corporate bankruptcies are seen as inevitable. It is expected that any faltering in the recovery will be met with further stimulative measures but governments have already significantly increased their budget deficits and their overall level of indebtedness potentially limiting their ability to respond. Further supportive action may extend the economic recovery which in turn could help maintain stock market valuations. However, further increases in debt levels also increase the level of risk for the future.

The economic recovery in some sectors may be relatively quick but others remain vulnerable to delays in the return to normality. It is the long-term damage to corporate as well as government finances that presents a significant risk to future economic stability. The outlook is further clouded by the increased tension between the US and China, and uncertainty with regards to the final agreement on trade or lack of one between the European Union and the UK. The low level of interest rates with negative rates in some countries does provide support for equity valuations but the debasing of currencies by excessive printing of money risks the eventual pickup in inflation. The strong run-up in the gold price over the last year and the recent acceleration in the rate of increase is a warning that the risk to financial stability may be underestimated.

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Manager's report for Scottish American – 14 August:

COVID-19 crisis has caused bond spreads to widen, and for the first time in some time, we have seen a number of interesting investments available.

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Bruce Stout, manager of Murray International – 14 August:

Unlike previous financial market dislocations, the underlying root cause of the past six months crisis - a global health pandemic - was interpreted by policymakers and politicians as a "nobody's fault recession". This allowed for unopposed, proactive intervention by the Authorities, unleashing a flood of liquidity into financial markets through interest rate cuts. Fiscal policy responses have also been unprecedented, with governments stepping in to underwrite wages for furloughed workers and providing emergency loans to support businesses. Capital controls are likely to tighten as the International Monetary Fund has been inundated with requests for aid, with many emerging economies facing the additional pressures of under-resourced health systems, soaring debt levels, and policy and de-globalisation challenges. Designed to prevent systemic economic collapse, such measures also had significant implications for the performance of stocks and bonds. Fixed income yields collapsed across the board, and numerous technology stocks, deemed to be beneficiaries of "social isolation", soared to unparalleled heights. The severity of dividend cuts from companies tackling evaporating revenues and profits has been the deepest on record. For global income funds, the backdrop could scarcely have been more difficult.

Asia

The region's swift and pragmatic response to the COVID-19 pandemic, combined with lower levels of debt and strong corporate balance sheets, augers well for recovery as economic restrictions ease.

North America

The US economy ground to a halt in April, with 95% of citizens locked down as the virus took hold. The Federal Reserve announced unlimited quantitative easing and the intention to keep interest rates near zero to 2022. US unemployment reached record highs of 14.7% in April before declining to 11.1% in June. Some corporates gained marginal relief from the fall in labour costs, helping offset the losses of weaker consumption. US corporate earnings were delivered with considerably fewer companies providing forward guidance. This resulted in downward revisions to consensus numbers broadly expecting further contractions in 2020 before a recovery in 2021, albeit still below pre-COVID-19 levels. Leveraged share buybacks are now likely to get more questions than support and many programmes have been suspended.

Europe

Europe began to emerge from lockdown as infection levels fell, but still faced OECD forecasts of 9.1% GDP contraction for 2020. The European Central Bank increased its asset purchase plan by 12% of GDP, with rates already negative. More recently, they signalled a pause in policy action as markets began to stabilise, and consideration of further expansion of the emergency bond purchase scheme.

UK

Emerging from lockdown towards the end of June, facing 2020 OECD forecasts of double-digit GDP contraction, the market has been brutally impacted by significant capital losses and the largest dividend declines of any global stock market. Ongoing uncertainty over future profit growth and dividend prospects as well as fraught post-Brexit trade negotiations provide a compelling case to remain cautious of the UK.

Latin America

Latin America endured a more torrid time as growth concerns weighed heavily on commodity-dependent economies such as Brazil and Mexico. Significant oil price weakness and the reality of impending recessions worldwide initially prompted investors to rapidly exit numerous emerging markets. With stability now re-established, the portfolio's Latin American exposure has begun to recover, but patience will be required before global confidence towards the region is fully restored. Scepticism towards emerging market equities was not replicated in the asset class's corresponding debt markets. Portfolio exposure to emerging market bonds experienced some days of intense volatility, but over the period, these bonds contributed very positively to relative capital performance and income accrual. Improving fundamental dynamics of favourable demographics, healthy savings and long term investment objectives in the emerging world continue to support and justify maintaining exposure to this attractive asset class within the portfolio.

Outlook

Markets are likely to remain volatile for the duration of the year. Expectations are for every major economy to contract, contending with slower growth, record low bond yields and companies struggling to achieve meaningful earnings growth, in the short term. The exit from lockdown will not be smooth and will be subject to periods of reversal.

Andrew Ross, chair of Witan – 11 August:

Although global equity markets have recovered much of the ground they lost, the recovery has been narrowly based. Technology and defensive sectors have done well, offsetting substantial losses by many other sectors. Although part of this is due to a reassessment of longer-term prospects (for example positive for technology, but much less so for office property and retailers), it also reflects a lack of confidence in the timing and degree of a cyclical recovery. Until there are more effective therapeutic treatments for COVID-19 or a vaccine, recovery hopes will remain vulnerable to secondary outbreaks, which might become more common as lockdown measures are gradually eased. The extreme performance differential between the 'COVID winners' and 'COVID losers' suggests that there is scope for a broadening out in stock market leadership when recovery confidence takes hold, while there is an increased burden of expectations built into the valuations of some technology companies. Those who recall the dotcom boom in 1999 know well that stocks can get ahead of themselves, even when the subsequent achievements of technology outstripped assumptions made at the time.

Flexible investment

(compare flexible investment funds **here**)

Peter Hewitt, manager of BMO Managed Portfolio Growth – 6 August:

For at least the next year, and in all likelihood longer than that, economic and stock market prospects will be heavily influenced by the nature of the recovery from the COVID-19 pandemic and how long-lasting the effects of the resultant recession prove to be. Another issue is whether a favourable trade deal can be struck ahead of the conclusion of the transition period before the UK's final exit from the European Union. There is also the uncertainty of a looming US presidential election. Also lurking in the background is the simmering rivalry between China and the US and whether we have a resumption of damaging trade wars or some form of accommodation which could reduce tensions. Although these issues are on the surface primarily medical and political, they will directly influence the economic outlook and also prospects for equity market returns.

The depth and rapidity of the economic contraction across the developed world is unparalleled in modern times and although economies are probably around the bottom currently it appears overly optimistic to believe that by the end of 2020 we will be back to where we were at the start of the year. From the trough, high levels of growth will be achieved in economic data but such was the extent of the decline full recovery will be some considerable time off. Once government support schemes unwind, unemployment could rise substantially and that also will impede recovery. It is uncertain how robust demand will be, particularly from the consumer, which is very important for the UK economy.

All of the above indicates that inflation will remain subdued, or even move close to negative over the next year and interest rates in the UK, Europe and the US will also remain at extremely low levels. This will be despite record levels of government spending and support which will continue for several years. Austerity is off the menu whereas higher levels of taxation be it corporate or personal may well be back on the agenda.

The remarkable rally in global equity markets from the lows of late March has been fuelled by Central Banks wishing to soften the effects of the inevitable recession. Quantitative Easing in the US, Europe, Japan and the UK has been substantial and has supported bond markets and indirectly equity markets. Eventually, however, longer-term returns from financial markets tend to be determined much less by political events or by policy from monetary authorities and much more by the outlook for the fundamentals of the economy and the prospects for corporate profits and dividends.

In this regard, corporate earnings reports for the second quarter/first half of this year will not make pleasant reading and although some modest recovery can be anticipated as we move through the year certain sectors, particularly consumer-related, will be very badly affected with many companies loss-making and some unfortunately not likely to survive. Equity markets have been focussing on 2021 and estimates appear to assume a robust recovery in profits and earnings in the UK, Europe and especially the US. It remains to be seen whether this is achieved. Valuations are elevated and require optimistic estimates to be achieved. In this environment, there appears ample scope for disappointment. Nonetheless, it is also important to remember the extent of monetary stimulus from Central Banks which is very supportive of both bond and equity markets.

In terms of long-term investment strategy, the case for exposure to sectors which offer secular growth characteristics remains in place. When inflation and interest rates are low and growth scarce then investment companies focussed on sectors such as technology, healthcare and biotechnology are likely to continue to prosper. That may change in the future as fiscal policy becomes an important tool for governments to stimulate economic growth and a more traditional cycle is created with higher inflation and an upwards move in interest rates. Investment companies with a more "value-based" investment style may then do better as more cyclical sectors such as industrials, retail, oils and banks experience a rally in their share prices.

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Richard Gubbins, chairman of Henderson Alternative Strategies – 4 August:

The social, economic and financial impact of COVID-19 has been, and remains, immense, with great uncertainty governing the shape of policy response and the nature and timing of recovery. With many individual businesses and certain business sectors requiring wholesale recapitalisation, with huge damage caused to fragile supply chains and with heavily dented consumer confidence, few business models remain truly unaffected. Some of these less damaged businesses sit within the alternatives space (certain 'availability' based infrastructure assets (an 'availability based' project allows a private infrastructure company to receive regular payments, per the agreed contract terms once the asset has been 'delivered and is available for use'. Payments are therefore not contingent on usage levels), for example) but equally some areas may see significant asset write-downs. For many illiquid asset classes, net asset values for the first quarter will not be available for some time and the full financial impact will take time to become clear. The consequence of such limited visibility is reflected in wider spreads for many assets (regardless of whether public or private), itself a function of lower volumes and more limited buyer availability.

Manager's report for RIT Capital Partners– 4 August:

As we enter 2020, we are cognisant that interest rates remain very low, which for some investors, makes equities the 'only show in town'. Our view is that a significant amount of good news is already priced in, and the market is unlikely to show resilience against any sustained macro or geopolitical volatility.

UK

(compare UK funds **here**)

Chun Lee and Robin Willis, managers of Acorn Income – 17 August:

Smaller companies

Given the nature of the pandemic and the subsequent government intervention, it is sectors and themes rather than individual companies which provide the greatest insight into activity and performance during the period. The managers took action early in the pandemic to identify and assess the threat to those companies within the portfolio that had increased end market risk and those with levels of debt which could become difficult to service in a prolonged period of lower economic activity. The leisure sector was particularly hard hit as operators were forced to close their doors to the public, effectively cutting their revenue to zero.

Income

Risk assets have staged a remarkable recovery from their lows in March following an unprecedented combination of large monetary and fiscal stimulus from global central banks. Corporate bonds, in particular, have received the most explicit central bank policy support with quantitative easing programmes actively buying, helping to maintain liquidity and to keep borrowing costs low in investment-grade bonds. Meanwhile, the fall in global interest rates and government bond yields has forced investors back into assets which were being indiscriminatingly abandoned merely a few months ago. However, while some pockets of the bond market overreacted in March, it has arguably been too optimistic in its interpretation of the recovery. We favour bonds from large, well-capitalised banks which are important conduits for central bank policy and much better placed to weather the downturn than many other businesses. Outside the banking sector, we like the relative resilience offered by areas such as supermarkets, telecoms and utilities, all supplying services which continue to be in demand. The more conservative management strategies being put in place in response to the pandemic should also mean that high-quality investment-grade companies prove to be a more stable and reliable source of income as discretionary equity dividends are cut in favour of maintaining contractual bond coupons.

The frenzied hunt for yield has also enabled global corporate bond issuance to hit record levels as companies look to take advantage of the yield-hungry environment and build liquidity buffers against the inevitable downturn. Issuance in sterling-denominated corporate bonds has however been much smaller in scale than the US Dollar and Euro markets, and deals have not looked as attractive. However, we have bought a few issues which were attractively priced relative to the market and to existing bonds issued by those companies.

Given the supportive technical backdrop, financial markets have been predominately focussed on the benefits of massive stimulus and less so on the risk to growth from the fallout of the pandemic, even as the US fails to control its infection rate. The second-quarter reporting season could therefore lead to a further weakening of credit metrics leading to more downgrades from credit rating agencies. While being respectful of the rally we also remain cautious given the worsening economic fundamentals which could lead to renewed volatility especially as the geopolitical tensions that were worrying markets before the pandemic - such as US-China trade relations and Brexit - are rising again, presenting threats to global trade as economies attempt to recover.

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William Meadon and Callum Abbot, managers of JPMorgan Claverhouse – 6 August:

A vast policy response from governments and central banks has, in the short term at least, averted the worst of the financial pain from COVID-19 crisis, leaving investors to gauge the long term costs and opportunities. Whilst asset prices have rebounded, the legacy of a heavily-indebted system weighs on growth prospects.

Much rests on what kind of economic and earnings recovery arrives in the post-pandemic world and whether stimulus packages can offset the damage inflicted by shutdowns. The sheer magnitude of central bankers' intervention suggests they are extremely concerned about long term economic scarring. They clearly worry that lingering economic weakness may soon become a problem for all. A negative real yield on 30 year US Treasuries suggests any recovery will be long in duration and modest in magnitude.

On a brighter note, it is already apparent that some companies and sectors are much better placed than others to cope with the enormous challenges ahead.

This is a global crisis like no other. Authorities around the world are currently walking a high-wire which is dangerously elevated and which has precipitous drops on both sides. In the continuing trade-off between lives and livelihoods, there are no silver bullets, only inexact exercises in probabilities and damage limitation.

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Manager’s report for Aberforth Smaller Companies – 4 August:

COVID-19 has cost thousands of lives and the threat of subsequent waves of the virus remains. It has also challenged societies and economies. Beyond its direct financial impact, the lockdown has exacerbated pre-existing issues, such as relations between the US and China, tensions within the US during an election year, existential questions for the Eurozone and populist unrest. Monetary and fiscal support programmes have mitigated the initial economic damage, but the extent of the eventual recovery in demand is uncertain: unemployment is likely to rise as businesses cut costs once furlough schemes end, which may affect the willingness of households to run high savings ratios back down. Prospects for the UK seem particularly unclear. This is reflected in sterling's leadership in the foreign exchange unpopularity contest, with 7% drops against both the dollar and the euro in the first half. Several of the attributes that have made the UK an attractive economy in which to invest seem under threat. Dividends have been slashed, pre-emption limits have been relaxed, the government has greater influence on the corporate sector and rules are being set informally without clear legislation. As temporary adjustments to cope with the impact of COVID-19, these are understandable, though a greater role for fiscal spending was likely even before the onset of the virus. The concern is that they herald more lasting changes at a time when the UK's future relationship with Europe and the future openness of its economy are moot. Of course, these are risks – they may not come to pass. Indeed, it is rare that the stock market does not have something to worry about. Admittedly, COVID-19 is a different type of risk compared with others experienced in recent years. At least in its early stages, its pathology was unquantifiable, and nothing shortens investment horizons like being forced to contemplate mortality. However, the world's reaction to the disease serves as a good reminder of where people – their efforts structured through societies and companies – excel. The significant advances in the understanding of COVID-19 in just a handful of months, along with economically costly but effective measures to control its spread, demonstrate human adaptability and ingenuity. Notwithstanding current outbreaks in parts of the US, it is not unreasonable to believe that any subsequent waves of the disease can be much less severe than the initial outbreak.

North America

(compare North American funds **here**)

Don San Jose, Dan Percella, Jon Brachle, managers of JPMorgan US Smaller Companies – 21 August:

While we believe the economy will eventually recover, we believe a higher-than-average period of uncertainty will persist until there is a viable cure for COVID-19. Through the volatility, we continue to increase our exposure to quality, focus on high conviction stocks, and take advantage of market dislocations for compelling stock selection opportunities.

We continue to focus on the fundamentals of the economy and company earnings. We estimate negative earnings growth for 2020 before a rebound in 2021, though we have low conviction in the magnitude of a potential rebound. We expect investor sentiment to remain subject to news regarding COVID-19 vaccines as well as the trajectory of key economic indicators, including employment. The upcoming US presidential election has the potential to add another layer of uncertainty.

Timothy Parton and Jonathan Simon, managers of JPMorgan American – 13 August:

While we believe the economy will recover, it will first need time to heal, and hence we remain balanced and continue to monitor incremental risks that could represent headwinds for U.S. stocks. Through the volatility, we continue to increase our exposure to quality, focus on high conviction stocks, and take advantage of market dislocations for compelling stock selection opportunities.

We continue to focus on the fundamentals of the economy and company earnings. Starting with profits, our current research suggests that profit growth could be around -23% for 2020, however, this figure has been trending upwards in recent months. Moreover, we do expect to have a strong recovery in 2021, and our current estimates are for earnings growth of +30% in 2021. While subject to revision, this forecast reflects our expectations for a very weak year yet ultimate recovery in the underlying economy and includes our best analysis of earnings expectations. Unemployment and other uncertainties, such as trade, fiscal stimulus, and the US election, will be integral to investor sentiment moving forward.

Europe

(compare European funds **here**)

Sam Cosh, manager of European Assets – 10 August:

The recovery has been surprisingly strong and as we write, almost the entirety of the sell-off losses have been recovered. Central banks and governments have provided enormous amounts of stimulus; coronavirus has begun to diminish in many areas and economies have started to reopen. Economic data is also reflecting this sharp rebound and central banks have made it clear that they are willing to do whatever it takes to keep government and corporate borrowing costs affordable.

Quality assets have led the rebound, but towards the end of the second quarter market leadership transitioned to value, perhaps indicating optimism towards a more sustained economic recovery. This, of course, remains to be seen but risks remain high. Firstly, the virus has not been entirely contained and a vaccine has not yet been approved. Even in places where infections had fallen to low levels, such as continental Europe, concerns of a second wave have surfaced while in the US and several emerging markets, the virus is not currently under control.

Political tensions also remain high, with US and China's diplomatic relationship challenging whilst the upcoming US elections provides a further level of uncertainty. Finally, we are reaching a stage where the massive fiscal support is now diminishing at the same time as economies are far from fully recovering.

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Manager's report for Fidelity European Values – 4 August:

Lockdowns, to control the spread of COVID-19, have, inevitably, resulted in significant downward revisions to economic growth forecasts. Encouragingly, however, this appears to have galvanised the European Union into action with the announcement, among other fiscal remedies, of a euro 750bn "Recovery Fund" to support its members' economies with a range of infrastructure and renewable energy projects. As always, the substance of the package will be subject to scrutiny and ultimate implementation, but the initiative has been greeted as a step in the right direction, particularly by investors wary of a new Eurozone crisis.

Shorter-term earnings and dividends for European companies have suffered substantial cuts too in the wake of the pandemic. Indeed, dividends have, unusually, proven even less resilient than earnings for a range of reasons including regulatory constraints in the financial sectors and political pressure to restrain payments to shareholders, particularly in France. Some companies have also not been able to pay dividends due to fundamental pressure on liquidity as revenues ground to a halt. While the equity markets' resilience, despite these downgrades to earnings and dividends, may suggest that investors view these reductions as transitory, the reductions in long term bond yields, and the liquidity being pumped into markets by central banks, will support the valuation of equities for some time to come.

Sector returns, in general, have diverged dramatically over the review period. Although the pandemic's impact on activity was the main determinant of performance, other factors also played their roles. Most notably, the growing focus on ESG standards influenced fund flows and sector performance too. Sectors such as energy, that were on the wrong side of both, performed particularly poorly. Technology, at the other extreme, was the outstanding beneficiary as the pandemic appeared likely to accelerate structural trends such as the shift to online and the digitalisation of companies.

The second half of this year is likely to be testing; not least because the pandemic is not yet over. Herd immunity or a vaccine are distant on the horizon so further waves and lockdowns appear inevitable. Central banks and governments are doing their utmost to support economies, and markets, but in doing so are potentially creating new problems for the future. Many companies that would otherwise have gone out of business will limp along, with reduced levels of staffing, such that many industries will continue to be oversupplied. Consumers are likely to remain wary and companies will hesitate before investing. Any economic recovery is likely to be fitful and anaemic. Equity markets have already bounced back strongly in the second quarter of this year so further progress will rely on a recovery in earnings and dividends much stronger than the manager currently anticipates, given that valuations, in aggregate, are already full. Presidential elections in the United States, not to mention the negotiations around a new relationship between the United Kingdom and the EU, have the potential to create moments of panic or relief in the second half of this year.

Asia Pacific

(compare Asia Pacific funds **here**)

Charles Clarke, chairman of Aberdeen Asian Income – 12 August:

While we have seen a rally in the second quarter of 2020, we have to be mindful of the disconnect between stock prices and corporate and economic fundamentals. We have yet to see a significant improvement in macro data and earnings that would justify valuations at these levels. I would not be surprised if markets reverse again. Governments are still walking the tight rope of having to re-open economies while trying to avoid a resurgence in COVID-19 infections. Several countries have already changed direction, even though they know that a re-imposition of containment measures would stymie the fragile economic recovery. For example, at the time of writing, the state of Victoria in Australia has just re-instated strict lockdown measures in the wake of a significant rise in infections. However, we expect continued fiscal and monetary measures to help support economies and markets.

Broader geopolitical risks further complicate matters, with tensions between China and the US a recurring theme. The rift started with trade but has since broadened to other areas. This is most evident in the technology domain, where the US wants to restrict China's global ambitions by limiting access to US technology. The manager is mindful of the potential repercussions, which could disrupt smartphone supply chains and delay the rollout of 5G networks. We also have an eye on the US presidential elections in November, which is shaping up to be an open race and with the outcome having a significant bearing on foreign policy.

In such a climate, it is no surprise that the outlook for corporate earnings has worsened. Many companies have lowered their profit forecasts, with dividend and capital spending being cut in certain cases.

Amid the uncertainty, it bears reminding that Asia continues to be well-positioned as the powerhouse of global growth. For one, we have the spending power of consumers in two of the world's most populous nations - China and India.

The region is also at the forefront of many exciting and emerging technological advances, such as vehicle electrification, Internet of Things and cloud computing. The region has the potential to offer investors good returns for many more years to come.

Global emerging markets

(compare global emerging markets funds **here**)

Manager’s report for Ashmore Global Opportunities– 21 August:

The general sentiment towards emerging markets has suffered under the strains of COVID-19 and resulting measures to fight the spread of the virus. Nevertheless, despite alarming headlines, most emerging countries are coping relatively well with lower rates of fatalities per million people than in many of the developed countries. We believe that is at least partially due to younger populations and less urbanisation, making social distancing easier. The IMF predicts shallower recessions and steeper economic recoveries in emerging countries compared to developed countries.

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Michael O'Brien, manager of Fundsmith Emerging Equities – 4 August:

COVID-19 is likely to significantly accelerate structural change across several industries, and we believe that the three biggest impacts will be formalisation, digitalisation and consolidation. Digitalisation, driven by the growth of e-commerce and changing working attitudes, will also positively impact on businesses which either provide services in these areas or are already enabled to serve e-commerce and modern trade channels. Although we aren't always necessarily fans of corporate activity, there may be opportunities for our holdings to consolidate their market positions and utilise their inherent strengths in areas such as distribution, by acquiring rivals who find themselves struggling for growth in a more difficult economic environment.

It is also broadly encouraging as an emerging market investor that the economic impact of COVID-19 on emerging markets (as measured as a percentage of GDP decline) is lower than that in the developed world, and most emerging markets are also forecast to revert to growth close to their long-term rate next year.

Japan

(compare Japan funds **here**)

Nicholas Price, manager of Fidelity Japan – 3 August:

Japan continues to offer an attractive combination of cash-rich companies, low relative valuations and secular growth opportunities.

India

(compare country specialist: Asia Pacific ex Japan funds **here**)

Manager's report for Aberdeen New India – 18 August:

it was an election year with the Bharatiya Janata Party (BJP) securing victory and Narendra Modi resuming his role as prime minister. This was viewed by many as a positive outcome as they expected continuity in the reforms which he had initiated. But events did not unfold as expected. The economy had already been facing several obstacles to growth. To boost consumption and encourage private investment, the administration lowered corporate tax rates and unveiled several measures, including credit support, especially for the automotive and real-estate sectors. The government also attempted to strengthen the financial sector, which had been experiencing defaults by non-banking financial companies (NBFCs). In so doing, several public sector lenders were consolidated and recapitalised in a bid to create scale and improve efficiency to produce a financial framework that would support both NBFCs and housing finance companies. As part of this fiscal assistance the central bank, the Reserve Bank of India (the RBI), relaxed monetary policy to support growth.

As with some miscalculations during Mr Modi's first term, such as the poorly conceived demonetisation policy, investors were concerned when the government revoked the special status of the state of Jammu and Kashmir and faced civil unrest with the proposed Citizenship (Amendment) Act, 2019.

At the turn of the year, investor sentiment was further dampened by the emergence of COVID-19. Investors were anxious over the economic impact on livelihoods resulting from countrywide lockdowns. Meanwhile, oil prices slumped on reduced demand. Exacerbating the situation was the breakdown of talks between OPEC and Russia, with their mutual failure to agree on supply cuts resulting in further rounds of falls. This also marked a surreal milestone with the West Texas Intermediate oil futures benchmark registering a negative price for the first time ever. While India is a direct beneficiary of lower oil prices as a net importer, it seems unlikely that this will be able to compensate for the impact of COVID-19 on the domestic economy.

To curtail the spread of COVID-19, India imposed a nationwide lockdown from 25 March 2020, in common with other countries. However, this caused the economy to grind to a halt. To ease the pressure on end demand, the government implemented a fiscal package which included cash pay-outs and food security for the more vulnerable. On the monetary front, the RBI cut interest rates and enacted a raft of other measures to maintain adequate liquidity in the system which was in danger of seizing up as businesses suffered from lockdown-induced disruption. Despite these measures, there will be a significant decline in overall growth this year.

Outlook

Amid the uncertainty which we have witnessed it is obvious that the disjointed and uneven application of policies across individual countries, as well as the lack of strong leadership to galvanise and coordinate efforts to fight COVID-19, may lead to further problems for the global economy. In India, while the implementation of the lockdown and subsequent measures appears to have been effective so far, the economic costs of COVID-19 have yet to be fully recognised. While the government's stimulus was aimed mainly at the lower-income groups that have been hit hardest, the initial response was somewhat underwhelming. This is partly because there are limits to how much further the government can loosen its fiscal purse strings, with its coffers already stretched heading into this crisis. Nonetheless, the government announced belatedly in mid-May 2020 a stimulus package to support small businesses and the rural economy. There were concerns that the lack of testing capacity could result in the under-reporting of actual infections which recognises that there was also a significant threat of a potentially wider spread as migrant workers returned to their villages from overcrowded cities. The manager remains cautious on India's ability to contain COVID-19, as well as manage the fallout, given the poor healthcare infrastructure.

For the longer-term, India exhibits several structurally positive trends in its favour. Foremost, it is home to many of Asia's most successful companies, a number of which have been stress-tested and have survived the previous economic and financial crises. It is also a beneficiary of a rapidly growing middle class that is both upwardly mobile as well as increasingly affluent.

Debt

(compare debt funds **here**)

Rhys Davies, manager of City Merchants High Yield – 21 August:

During February and March, as economies were shuttered, credit spreads (the premium over government bonds that companies need to pay to borrow) widened significantly. The credit spread of the ICE Bank of America European Currency High Yield Index was 324 basis points (bps) at the start of the year. After tightening in January and February, spreads then widened to reach a peak of 884bps in late March. This was its widest level since the height of the eurozone sovereign crisis in 2011 and resulted in the index delivering a Q1 sterling hedged total return of –14.6%.

The deterioration in sentiment was compounded by a collapse in the oil price that followed the start of a price war between Saudi Arabia and Russia at the beginning of March. This was more significant for the US high yield market, which has a high allocation to the energy sector.

From late March sentiment turned with European high yield delivering a sterling hedged total return of 11.35% – its best quarterly return since 2012. This occurred despite the release of some of the worst economic data ever recorded. The reason for this turn in sentiment was the extraordinary monetary and fiscal policy response of central banks and governments.

The US Federal Reserve, in particular, has gone well beyond the remit of its previous quantitative easing programme to directly purchase corporate bonds. These purchases include bonds downgraded to high yield after the pandemic began. In Europe, the European Central Bank increased its bond purchases, but significantly there was also a proposal for a fund in which the nations of the eurozone would jointly borrow to help fight the pandemic. A €750bn recovery fund of both grants and loans has since been agreed.

Against this backdrop corporate bond issuance levels have soared as issuers have sought to take advantage of the demand for yield to build up cash surpluses and repair their balance sheets. Indeed, Bloomberg report that June 2020 was the busiest ever month for US high yield issuance.

By 30 June 2020, European currency high yield credit spreads had recovered from the wide levels of late March to a level of 541bps. Although below the March peak, this level is still well above the average for the past decade. It was a similar story in the US market with spreads widening from 554bps at the start of the year to 1087bps in late March before falling back to 647bps by 30 June 2020.

Outlook

As we look ahead, we are cognisant that the main driver of the current rally in financial markets has been the unprecedented monetary and fiscal policy support. The message from central banks and governments is that this support is not likely to change in the near term. Therefore, while it is difficult to see markets moving much higher, it is equally difficult to see a catalyst for any significant sell-off.

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William Scott, chairman of Axiom European Financial Debt – 21 August:

The effect of COVID-19 has been profound and its impact on some sectors nothing short of a disaster; for others, it has been a bonanza. The full effects will take time to flow through fully and manifest themselves in the balance sheets of banks. It is pleasing to note that the recovery in the economy seems at present to be quicker than might have been feared. We must, however, recognise the possibility that there will be future "waves" of the pandemic and it will be some time before the pandemic can be declared "over". In the meantime, we also should bear in mind that the major themes that concerned markets before the pandemic are still there, even if they are not so prominent in the news as they would otherwise have been: the US-China trade tensions, Brexit, and of course the regulatory change in the financial sectors.

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Manager's report for Riverstone Credit Opportunities Income– 13 August:

The current macro environment for energy continues to face a significant amount of volatility as the coronavirus pandemic continues to persist globally. While spot prices for oil have modestly improved, the uncertainty around global demand remains and continues to impact the broader energy market. In light of the current market dynamic, many companies will need access to capital and have limited options for financing.

Private equity

(compare private equity funds **here**)

Manager's report for Apax Global Alpha – 25 August:

The impact on the global economy has been severe. US real GDP fell by c.10% during Q1 2020, with EU real GDP falling by c.12% during the same period. Policymakers responded with unprecedented fiscal and monetary stimuli which have mitigated potential worst-case scenarios. As economies opened up in the US and Europe during May and June, we have seen a rebound in economic activity. However, it remains very unclear at what rates, and by when, most businesses will recover to pre-COVID levels. If we look at China as a lead indicator, economic activity is still below pre-COVID levels. There has also been a significant divergence in economic performance by both sectors and geographies with businesses impacted and recovering at different rates.

Private equity update

In private equity markets, the volume and value of transactions were materially down in H1 2020 vs 2019. However, there was perhaps more deal activity than might have been anticipated. At the start of the crisis, some private equity investors saw the opportunity to invest into public equities to provide capital for structurally sound but COVID-19 impacted companies via so-called private investments in public companies (PIPEs). As confidence returned somewhat towards the end of Q2 and financing for transactions became available, more traditional leveraged buyout transactions were completed.

Valuations for quality companies continue to be elevated with the private equity market heavily discerning between those companies viewed as structural winners (e.g. software) and those considered more structurally challenged (e.g. "bricks and mortar" retail).

Credit market update

Credit markets somewhat mirrored equity markets though H1 2020. Through central bank action and an investor flight to safety, government bond yields compressed to historic lows across the yield curve. With euro base rates having been at or below zero for extended periods, the yield curve in the US tightened significantly following the outbreak of the crisis.

Simultaneously with public equity markets seeing significant losses in March, credit spreads widened materially for investment grade, high yield and leveraged loans. In particular high yield and loan markets dislocated severely, with prices for loans in high-quality companies dropping materially in line with the broader markets.

However, spreads narrowed again through Q2 as investor confidence returned and fiscal and monetary stimuli were announced. As in public equities, investors distinguished between what was perceived to be higher and lower quality sectors and companies in the current crisis.

As might be expected, new issuance volumes for credit supporting leverage transactions were very low at the outset of the crisis, but these returned during Q2 2020 which also saw signs of second lien loans re-emerge.

Outlook

The economic outlook remains highly uncertain. While countries have begun to rebound as they have reopened from lockdowns, levels of GDP remain well below pre-COVID levels in most economies. The speed of recovery will depend on the evolution of the pandemic, medical interventions, policy responses, and general consumer and business confidence. The recovery is unlikely to be linear and, for most economies, economic activity may not return to pre-COVID levels until 2022.

Valuation levels for equity markets are at elevated levels and generally assume earnings normalise to 2019 levels by 2021. This is somewhat driven by very low bond yields and a lack of attractive liquid investment alternatives indicating that valuations may remain elevated for the foreseeable future. Valuations will also likely continue to be superior for those companies viewed as better positioned through COVID-19 compared to those which are more impacted or structurally challenged.

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Hamish Mair, manager of BMO Private Equity – 21 August:

The second half of the year should provide a stronger economic background as easing of lockdown measures internationally allows economies to pick up. Whilst the trend is one of improvement there remain huge challenges and uncertainties. All but a handful of portfolio companies are adversely affected but the degree of disruption varies considerably across the sectors. Some sectors are adapting much more easily to working from home than others, for example, software companies. It is also the case that demand is proving resilient in essentials such as food and healthcare. Companies which rely on experiences such as much of retailing, performing arts and travel are greatly disrupted and face an ongoing crisis.

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Manager’s report for Princess Private Equity – 17 August:

The uncertainty and risk created by COVID-19 continues to affect corporates and the global economy. On a macroeconomic level, indicators suggest that the trough in output was reached in the second quarter in most parts of Europe and the US. Purchasing Manager Indices have also started to paint a more positive picture and the US labour market has beaten expectations for job growth in both May and June. We have further witnessed some stabilization in the revision to economic forecasts and corporate earnings in the latter half of the second quarter.

However, millions of people remain outside the workforce, supported by government wage subsidy programs which are due to expire. Rising new COVID-19 cases in different countries and regions around the globe have resulted in an extension or reintroduction of lockdowns, which may slow the global recovery process. Reflecting these developments, Partners Group continues to monitor the performance of portfolio companies closely and stands ready to support them as required.

Following a slowdown in investment and realization activity during the second quarter of 2020, there are signs that transaction volumes are slowly increasing.

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Manager's report for Pantheon International – 6 August:

While we are cautious on the near-term outlook, it should be remembered that private equity is long term and flexible in nature.

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Manager's report for LMS Capital – 4 August:

The first half of 2020 has been an extremely volatile period as global financial markets and businesses have been dominated by the impact of the Coronavirus pandemic. In the UK, the economic uncertainty from the Coronavirus pandemic was compounded by the ongoing Brexit trade negotiations with the European Union. UK equities hit a year-to-date low on 23 March when the UK government announced the lockdown over the pandemic. Both the UK Aim and Small-cap indices declined over 28% during the first quarter. The Bank of England has provided massive stimulus packages through the expansions of its bond repurchase policy and reduction in interest rates, and the UK government has supported employment through state-funded furlough schemes. The domestic markets rebounded during the second quarter, but the UK Aim and Small-cap indices are still down 8% and 16%, respectively, from their end of 2019 levels. The US Dollar also strengthened against the sterling during the first half of 2020.

Hedge funds

(compare hedge funds **here**)

Bill Ackman, manager of Pershing Square – 28 August:

We are entering an era in which we expect the dominant, well-capitalized, great companies to accelerate their growth in market share and profitability over the long term as they effectively adapt to the changes wrought by the virus. While many have been puzzled by the stock market's resurgence, in our view, it can be best explained by this phenomenon writ large. Said differently, we have a corporate inequality phenomenon in addition to an income inequality problem. The stock market is comprised of the biggest and strongest companies and reflects the present value of what is to come for these businesses. It is not representative of the entire economy. If there were a stock market index of private, small businesses, it would likely be down 50% or more. Small business failures will make the income inequality problem even worse. If we are to avoid continued political risk and disharmony which create serious risks to the sustainability of the capitalist system, we need to find a way for those left behind to participate to a greater extent in capitalism, broadly defined. This is an important problem that must be addressed, and it is incumbent upon all of us, particularly those of us who are the greatest beneficiaries of the system, to find a potential solution. Despite its faults, we are strongly of the view that, while far from perfect, capitalism is by far the best system for maximizing the size of the economic pie. One of the principal problems with capitalism, particularly as it has functioned over the last several decades, however, is that wage growth has not kept pace with long-term wealth creation, which has disproportionately favoured the wealthy and the upper-middle class. This likely can be attributed to the higher after-tax returns generated by investment assets compared with wage growth over the same period. Without funds to invest for retirement – particularly after the housing crash destroyed many Americans' only other source of long-term wealth creation – one has almost no hope to build wealth for retirement or to give the next generation a head's start. In sum, the American Dream has become a disappointment or worse for too many. If capitalism continues to leave behind most Americans as the growth in wages has not come close to the more tax-efficient compound growth that has been achieved by investing in the stock market, more and more Americans will seek changes, potentially radical ones, to the current system, or seek an alternative system. Like those who rent rather than own their homes and thereby have no love lost for their landlords, Americans that have no ownership in the success of capitalism, and who are suffering economically, are more motivated to turn toward Socialism or other alternatives. One potential solution to the wealth inequality problem is to create a way for those with no investment assets to participate in the success of capitalism. We need a program that makes every American an owner of the compounding growth in the value of corporate America. Compounded returns over time are indeed one of the great wonders of the world, and every day we wait to address this issue, the problem looms larger. There are a number of potential solutions to this problem. Among them, the government could establish and fund investment accounts for every child born in America. The funds could be invested in zero-cost equity index funds, be prohibited from withdrawal until retirement, and could compound tax-free for 65 years. At historical rates of equity returns of 8% per annum, a $6,750 at birth retirement account - which would cost $26bn annually based on the average number of children born in the U.S. each year - would provide retirement assets of more than $1m at age 65.

Alternatively, or hopefully, in addition, corporations could be required to set aside a fixed percentage of salary or wages in a tax-free investment account for all workers that would also be restricted from withdrawal until retirement, similar to the approach used by the highly successful and popular Australian superannuation system, which has created savings of scale for growing generations of its citizens. Since the superannuation system's launch in 1991, Australia now has $2.7trn of superannuation assets – nearly twice the country's GDP. Remarkably, Australia has created the fourth largest pension system in the world, in the 53rd most populous nation. In addition to helping all Americans build wealth for retirement, mandatory equity savings accounts for all would encourage greater financial literacy, and, as importantly, allow all Americans to participate in the success of capitalism. We are not going to solve our country's problems in a few short paragraphs, but we highlight the above problems as they are critically important for the country to address, and, like COVID-19, they present black-swan-type risks for investors. These and other issues of global concern, like climate change, create substantial unresolved risks and uncertainties.

Manager reports for BH Global and BH Macro – 26 August:

Global growth had been on a slowing trajectory through 2019 and, as we entered 2020, the Master Fund was positioned in anticipation of potential easing by the US Federal Reserve with the view that the market was underappreciating the potential for policy action. As the COVID-19 crisis began to unfold in February, we anticipated that it would cause unprecedented economic devastation and equally unprecedented fiscal and monetary policy responses. In the event, the global economy is estimated to have contracted by as much as in the first year of the Great Depression and by more than in the Great Financial Crisis. In response, most countries delivered sizable fiscal relief, while most central banks cut rates to nearly zero, restarted quantitative easing, and rolled out a wide variety of ambitious lending programs — measures that provided a safety net for stocks and credit. During this period, the Master Fund added to directional and relative value strategies across a range of global interest rate markets. The Fed was forced into making two emergency cuts totalling 150bps and risk markets fell sharply. Gains over this period came from a range of strategies including directional trading of US and global interest rates, spread trading in European government bonds, LIBOR-basis and option volatility positioning as well as from directional and options strategies in equity, credit, oil and precious metals. Moving into the second quarter, gains were crystallised, risk levels reduced, and the Master Fund adopted a less directional and more tactical approach. Some gains were generated from recovery trades in credit markets and commodities although these were offset by modest losses in rates and FX.

Looking forward, financial assets are expensive by many standard metrics. So long as a V-shaped recovery in risky assets fails to create a V-shaped recovery in economic activity, this tension is a recipe for increased volatility. In the past, a gap like this between ebullient market pricing and sobering fundamentals has sometimes presaged abrupt non-linear adjustments. But since interest rates are constrained by the zero lower bound and credit spreads have been explicitly underwritten by major central banks, volatility will have to show up in other asset classes. Currencies and traditional hedges like precious metals may act as a barometer of the success or failure of policy responses to restore economic normalcy. The November presidential election is one specific focus. Joe Biden recently declared that “it’s way past time to put an end to the era of shareholder capitalism.” If the Democrats sweep the White House and Congress, the outlook for US Dollar assets will come under increased scrutiny.

Technology & media

(compare technology & media funds **here**)

Walter Price, manager of Allianz Technology – 3 August:

In our view, the technology sector continues to benefit from strong tailwinds which should continue to drive attractive long term appreciation. There is no question in our minds that the present events around the COVID-19 crisis will spur the use of technology and change how we live and work in the future. As companies adjust budgets due to supply and/or demand disruptions, the need for companies to reduce costs should accelerate the move to cheaper and more productive solutions such as cloud, software-as-a-service, artificial intelligence, cybersecurity, etc. We are in a period of rapid change, where the importance of technology is key to the prosperity of most industries. Looking ahead, this environment is likely to provide attractive growth opportunities in many technology stocks.

Infrastructure

(compare infrastructure funds **here**)

Manager's report for BBGI SICAV – 28 August:

Some governments are seeing the current situation as a valuable chance to improve infrastructure and expand economic opportunity. Lower interest rates make borrowing cheaper compared to recent years, reducing the upfront costs of generational projects. Infrastructure spending can also create immediate professional opportunities across a mix of design, construction, and operational jobs. The mix of short-term employment and long-term investment makes infrastructure an attractive area for countercyclical fiscal stimulus. We expect this to be the theme in many of the markets where we are active including Canada, US, UK and Europe.

Canada

The Investing in Canada Infrastructure Program is being adjusted so that provinces and territories can use federal funding to act quickly on a wider range of more pandemic-resilient infrastructure projects. Under a new COVID-19 Resilience funding stream worth up to $3.3bn, projects will be eligible for a significantly larger federal cost-share and a simplified funding application process will ensure that projects can get underway as soon as possible. These changes are designed as short-term measures to address the current situation while the Federal Government works towards its long-term infrastructure objectives, including better public transit, more high-speed broadband, wastewater infrastructure and clean energy projects.

UK

In the UK, the Chancellor's 'Plan for Jobs' issued in July 2020 set out the UK Government's policy response to help the economy recover from the COVID-19 lockdown, following the infrastructure investment plans announced by the Prime Minister the previous week. The £30bn fiscal package includes £5.6bn of infrastructure spending which has been brought forward from future years' budgets.

US

In the US, there are expectations of support for increased infrastructure spending. There is little doubt about the political and economic value of investing in good infrastructure. The non-partisan Congressional Budget Office estimated that every $1 on infrastructure brought an economic benefit of up to $2.20. The US Council of Economic Advisers has calculated that $1bn of transportation-infrastructure investment supports 13,000 jobs for a year.[xiii] We are expecting that infrastructure spending will be a key foundation for economic recovery going forward, irrespective of which party is elected in November 2020.

EU

In July 2020, the European Union's executive arm announced a €750bn stimulus plan which includes funds earmarked for sectors of strategic importance such as critical infrastructure and healthcare.

While the prospects are promising for increased infrastructure spending in many markets, this is not a universal theme.

Australia

Some governments are cutting infrastructure projects due to expectations of reduced sales and income taxes. As an example, the State of Victoria in Australia recently cancelled the A$2.2bn arterial roads PPP. The Australian Government has said it favoured a more 'streamlined' procurement process which breaks up the work into 12 contracts with smaller, local construction companies, which it believes would be a better way to add more jobs during the COVID-19 related economic downturn.

Ongoing secondary opportunities

Historically, construction companies have been a good source of investment opportunities for BBGI. Amid the tough operating environment triggered by the COVID-19 pandemic, and the general slowdown in construction activity in many markets, the management board anticipates that many construction companies may accelerate their plans to sell PPP assets. BBGI was able to acquire interests in the Stanton Territorial Hospital project from two construction companies who were partners in the project. We anticipate this trend to continue.

2020 and beyond:

Investment activities in 2020 and beyond will involve sourcing and originating, bidding for and winning new operational availability-based assets, with consideration for measured exposure to construction assets to support valuation uplift.

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Manager’s report for Premier Global Infrastructure – 5 August:

Energy efficiency and renewable financing will be increasingly important as companies seek to cut emissions generated in industrial property and processes.

Renewables

(compare renewables funds **here**)

Manager’s report for Renewables Infrastructure – 7 August:

Power demand

Power demand fell across TRIG's key markets during the period. Reflecting the mild winter and the severity and timing of COVID-19 measures, power demand was significantly reduced at the peak of movement restrictions across

In the UK, the average demand is running approximate 10% below 2019 levels. However, power demand has been increasing as lockdown measures have eased.

Such an unanticipated and prolonged reduction in demand has consequences for how the energy system is managed. In particular, balancing the grid during times where generation exceeds demand has been challenging for system operators, increasing the likelihood of grid curtailment or constraints. These challenges have raised awareness of the need for greater grid infrastructure investment across the markets.

In GB, National Grid has introduced the Optional Downward Flexibility Management (ODFM) service, in addition to its established Balancing Mechanism (BM). This scheme allows embedded generators to be compensated when asked by National Grid to stop generating to help match electricity supply and demand and to support network resilience.

Power prices

As a consequence of the fall in demand for electricity and other commodities, particularly gas and lignite, power prices have fallen. These commodities are important as they set the market for power prices in the UK and Germany respectively, with the German market, in turn, a price-setting country for European interconnected power flows.

The Green Recovery Opportunity

One of the few beneficial consequences of the reduction in activity caused by the COVID-19 pandemic has been the short-term reduction in carbon emissions globally and improved air quality. Global daily CO2 emissions reduced by 17%1 by early April 2020 compared with average emissions from 2019 and, at their peak, emissions in individual countries fell by 26% on average. With a clear and pressing need for economic stimulus to drive economic recovery, there is broad political support in the EU and the UK to use recovery funds as a means to drive forward the energy transition to a future without greenhouse gas emissions.

The European Green Deal, announced before the widespread outbreak of COVID-19, is now central to the European Commission's economic recovery plans. These plans include investing in various policy areas including €25bn into renewable energy between 2021 and 2027. Many of the Green Deal initiatives will not only necessitate renewable energy to displace fossil fuel demand but will increase the overall demand for renewable electricity, for example through the electrification of transport.

The UK government is now holding Presidency of the UN COP26 Climate Conference, has announced an urgent drive to start projects that are ready for construction, including renewable energy infrastructure, to increase investment and economic activity. In addition, in March the UK government set out details of the next Contract for Difference (CfD) round for 2021. Importantly, the government announced that this will be open for "established" technologies including solar and onshore wind.

Political Risk - Brexit

The UK left the EU on the 31st of January 2020 and then entered into the transition period. The period during which an extension could be requested to the transition period for the UK exiting the EU expired at the end of June, in accordance with the Withdrawal Agreement, suggesting that both parties now must agree on a trade deal by December 2020. With the UK officially leaving the EU's internal energy market at the end of the year, both the UK Government and European Commission have stated that they are keen on maintaining a strong co-operation on energy policy and will establish a new energy trade.

Environmental

(compare environmental funds **here**)

John Scott, chairman of Impax Environmental Markets – 4 August:

The health and economic impacts of the pandemic have highlighted areas of structural weakness in the global economy, particularly in relation to sustainability and vulnerability of supply chains. By contrast, they have also revealed areas of remarkable resilience, particularly in companies supplying basic needs to the consumer. Lockdown conditions have prompted what may turn out to be a structural shift in work patterns towards home-working, facilitated by a dramatically increased use of technology, and accompanied by permanently altered patterns of consumption.

Importantly, notwithstanding near-term volatility seen in some of the sectors in which the Company invests, we believe that the structural changes arising from COVID-19 are likely to reinforce the investment hypothesis underlying IEM.

These structural changes include an acceleration of the transition away from carbon-intensive industries that were underway before the pandemic. Unlike during the 2008-09 financial crisis, environmental considerations have been a prominent feature in many of the stimulus packages - totalling so far around $9trn - that governments have launched to protect incomes and businesses.

For example, the EU has pledged that 30% of its €750bn recovery plan will be directed towards climate action, while China announced a 'New Infrastructure' investment programme focused on electric vehicles, low-carbon transport, 5G networks and an upgraded electrical grid.

In addition, the lockdown has resulted in dramatically and visibly improved air quality in many of the world's most polluted cities, with measurable health benefits. While some of these improvements in air quality will be short-lived - and have been achieved at unsustainable economic and social costs - they have triggered a debate about what levels of pollution are acceptable and have perhaps brought home to people how much damage has already been done to the environment. Data suggesting that COVID-19 mortality rates are higher in areas with high levels of air pollution will add grist to those discussions and, ultimately, help to support IEM's investment thesis.

Reduced demand for oil due to lockdowns, exacerbated by squabbles between Saudi Arabia and Russia, has led to oil prices falling dramatically during the Period. A low oil price will, at the margin, weigh on the economics of energy efficiency investments in some markets but, in contrast to similar episodes in the past, there is as yet no indication that cheaper oil is leading to sell-offs in renewable energy firms. Today's investors understand that oil and power prices are no longer closely correlated and renewable energy-focused utilities have outperformed during the recent turbulence. Indeed, it has been notable how oil majors have announced write-downs in the value of assets during the period, partly because the pandemic is likely to have brought 'peak demand' for oil closer, as remote working habits and local air pollution concerns linger. The fact that we are even discussing 'peak (oil) demand' is remarkable, given that only a few years ago the focus was on 'peak supply'.

The pandemic has revealed the fragility of human society in the face of a natural phenomenon and has triggered the kind of collective response that will be needed to address climate change and other sustainability challenges that we face.

Outlook

Market conditions may well be volatile over the coming months. Investors will be watching closely for the development of vaccines or effective treatments that can halt or at least blunt the pandemic. The effects of the coronavirus in developing countries and the risk of further waves of infection in those countries that have been able to contain the virus risk provoking renewed downturns.

The pandemic has revealed the fragility of human society in the face of a natural phenomenon and has triggered the kind of collective response that will be needed to address climate change and other sustainability challenges that we face.

Commodities and natural resources

(compare commodities and natural resources funds **here**)

Evy Hambro and Olivia Markham, managers of BlackRock World Mining – 19 August:

During the first half of 2020, the spread of returns within the commodity complex has been as wide as we have ever seen. Iron ore prices remained rock solid throughout the period, as ongoing supply issues in Brazil kept markets tight despite the COVID-19 led recession. Gold prices have been stellar due to the move to near-zero interest rates across the world and the weak US dollar. Finally, the price of palladium moved to unprecedented levels on the back of supply concerns and improved loadings in heavy-duty vehicles. These rises are in stark contrast to the large falls in base metals prices during the period. Miners of zinc, tin, aluminium, copper and lead saw double-digit percentage falls in average prices year-on-year leaving some metal prices below marginal costs of supply, for example, aluminium where capacity is being closed by key supply producers such as Rio Tinto. Coal miners also suffered as prices fell deep into the cost curve on the back of ongoing cuts to demand, as the world transitions more rapidly towards a lower-carbon economy.

On the back of the wide range of moves in metal prices, the spread of returns in the equities has been equally wide. Amongst the industrial commodities, key holdings such as Rio Tinto, BHP and Anglo American have materially outperformed others with greater exposure to base metals such as Glencore. In addition, non-copper producers have fared far worse than key holdings in Freeport-McMoRan Copper & Gold, Lundin Mining and Antofagasta. Finally, the gold equities outperformed almost all other holdings as margins and cash flow meaningfully expanded as the gold price rose and by the end of the period our position in gold companies had risen to 35.2% of the portfolio (31 December 2019: 23.2%).

In addition to commodity prices, the geographic location has been a significant driver of returns as governments imposed different restrictions on mining operations in response to COVID-19. For example, in Australia, iron producers have been able to operate at close to full capacity throughout the period, versus producers in Peru, South Africa, Mexico and Canada that were forced to reduce people at site and mining rates in response to the virus. We have also seen a large divergence in demand by geography, the most notable in steel, where Chinese steel demand has recovered strongly underpinning demand for iron ore, whilst European steel demand has waned putting pressure on coking coal prices which were down by 43% during the first half of the year.

Amidst the commodity price volatility in the first half of the year, margins have generally held up better across the sector given the absence of cost inflation. The sharp move down in oil prices and commodity currencies such as the Brazilian real and South African rand, has helped to buffer the downward move in prices year to date. Anglo American and Vale have enjoyed a strong tailwind from foreign exchange rates this year and we expect this to become apparent in the second half as operating volumes improve for both companies.

Dividend-led rotation?

In recent reports we have emphasised and applauded the improved capital discipline across the sector, which today sees the sector with one of the strongest balance sheets globally, enabling the companies to offer an attractive dividend yield to investors. Since 2018 we have seen a step up in returns via dividends and last year we saw record dividends paid by BHP and Rio Tinto due to a combination of high iron ore prices and asset sales.

Given the dividend challenges faced by companies globally and especially in the UK, versus the market’s ongoing desire for yield, we believe there is potential for investors who are desperately searching for income to increasingly look towards this sector for income. Should this come to pass it might trigger a rotation of capital from other sectors back into the mining shares and in turn compress the dividend yield premium that the mining sector trades on.

As we look towards the second half of the year, we remain broadly optimistic on the outlook for dividends particularly for the iron ore exposed diversified miners given the strength in prices year to date. The absolute level of dividends will be ultimately dictated by the underlying commodity prices. However, given balance sheet strength, the limited calls on growth capital and companies’ strong commitment to adhere to their capital allocation strategies, we continue to believe the mining sector can deliver a healthy level of income for shareholders. To date, we have seen limited dividend cuts across the sector, with Glencore (not in the portfolio) cutting its dividend, Antofagasta reducing its announced dividend and Freeport-McMoRan Copper & Gold cutting its quarterly dividend in March, as the copper price bottomed. Conversely, we have seen strong dividend increases from a number of gold companies with Newmont Corporation raising its quarterly dividend by 79% and other smaller players doubling dividend payments. Today, the gold companies trade on modest dividend yields in absolute terms; however, given the increase in free cash flow generation this year, we look forward to higher distributions coming through and with fixed income returns setting a low bar maybe even a premium yield is reached.

Sustainable Metals

The shift towards electric vehicles (EVs) is one of the strongest trends we foresee. We expect a more than 10-fold increase in the size of the market by 2030, which creates growth opportunities for those companies supplying the materials that enable that transition.

Transportation has been impacted by the COVID-19 pandemic given the significant restrictions imposed on the movement of individuals over recent months. The sale of new vehicles has been significantly affected, with passenger car sales falling 80% year-on-year at the trough in both China and Europe. Encouragingly, sales in China have rebounded sharply and there is evidence in China that the virus is encouraging people to favour car ownership to avoid the use of public transport.

Looking ahead, the outlook for the theme may have been strengthened by recent events. More importantly, we are seeing government stimulus focused on restarting economies post lockdown, target sustainable themes, with EVs an important pillar of that, which has the potential to further accelerate the transport revolution. In Europe, for instance, the market share of EVs has increased every month so far this year and overall, the year to date share of EVs is around 7%, which is more than double what it was in 2019.

In China, the government has extended its subsidies for EVs by two years. In Europe, France has increased its EV subsidies by over 15%. Germany has gone even further, announcing a doubling of its EV subsidy and a temporary reduction in VAT, and has mandated that refuelling stations install EV charging points. The decision by the German government to only introduce automotive support measures for EVs is an incredibly powerful message about the industry’s future direction.

The main raw materials that go into EV batteries are cobalt, nickel and lithium. For cobalt we saw a price recovery, post a weak second half in 2019, with London Metal Exchange prices up by 12.9% in the first half of 2020. Last year Glencore acted to balance the cobalt market with a decision to suspend the Mutanda project in the Democratic Republic of Congo for two years, impacting 20% of global supply. In April, Glencore announced the acquisition of Katanga Mining from the minority equity holders, including the Company. This transaction was completed in June 2020.

Lithium prices moved lower throughout the year, down 27% in the first half of 2020. As well as the tempered growth outlook, prices have been hit by the increased supply of Australian lithium concentrate. Prices continue to be low enough for supply to be exiting the market and projects to be halted. In March 2020, we saw China’s Tianqi Lithium postpone commissioning of their Australian lithium conversion project in Kwinana and we have also seen Albemarle cut capital expenditure and delay projects whilst preserving optionality. The Company exited Albemarle during the first half of the year, redeploying this capital into other opportunities. The Company continues to be exposed to lithium through its holdings in the Pilgangoora Bond and Neo Lithium. Another major battery metal is nickel where demand is likely to benefit from the increased penetration of EVs and thus demand for lithium batteries which contain nickel in the cathode of the battery.

2020 has seen growing excitement about the potential for hydrogen to disrupt the commercial vehicle market. Compared to batteries, hydrogen and fuel cells offer better energy density, improved range and faster refuelling, giving them an inherent advantage in efforts to decarbonise the heavy truck market. That said, there are substantial hurdles to overcome, with costs needing to fall dramatically for the switch to be economic. We see the technology's long-term potential but believe that we are still in the early stages of its development. Technologies involving platinum are crucial to the adoption of hydrogen fuel cell and electrolyser technologies. The Company's positions in Impala Platinum, Northam Platinum, Anglo American and Norilsk Nickel provide exposure here.

Given the rapid response from central banks and governments, financial markets have reacted well to the support mechanisms put in place. The next phase is a balancing act between restarting the economy, whilst trying to minimise a sizable second wave virus outbreak. At the time of writing, the fiscal measures that have been announced are extremely supportive for growth and should the dollars be deployed in a reasonable time then industrial commodities are likely to benefit from this.

Unlike in previous periods of economic disruption, the mining sector has fared much better largely due to the time spent rebuilding the businesses post the 2015 low. With first-half results highlighting the strong cash flows and decent yields, there is the prospect that those investors looking for quality equity income investments rotate into the resources sector allowing the consensus underweight positions to reduce. If this happens, the shares are likely to rerate towards historic multiples delivering material upside from current levels.

Manager's report for Riverstone Energy – 19 August:

WTI prices experienced unprecedented headwinds due to concerns around supply and demand dynamics resulting from the coronavirus pandemic. While OPEC+ agreed to production cuts after an initial standstill in March, the decrease in demand due to coronavirus has continued to weigh down oil prices. WTI ended the period at $39 per barrel, while forward strip prices remain approximately $20 per barrel below levels seen at the end of 2019.

At the end of the first quarter, energy markets faced numerous challenges resulting from a failed OPEC+ agreement on production cuts, coupled with the severity of the coronavirus pandemic. These coinciding events caused spot oil prices to drop dramatically to a low of approximately negative $37 per barrel in April 2020, as traders began offloading inventory as storage challenges emerged. Forward prices also decreased dramatically, with the one-year strip price declining by $22 per barrel during the period compared to the end of 2019.

In response to cratering oil prices, OPEC+ agreed to cut 9.7m barrels a day, the deepest ever agreed upon, during May and June, which helped to boost oil prices as demand for crude began to recover with the slow increase in economic activity. Furthermore, U.S. shale producers significantly curbed production as low prices created uneconomic drilling conditions and companies drastically reduced capital expenditures. U.S. field production, as reported by the EIA, reached peak production of 13.1m barrels per day in March 2020, but has since been reduced to 10.5m barrels per day as of June 2020, representing a decrease of approximately 2.6m barrels per day. This represents the lowest U.S. production volumes since October 2018.

During this challenging period, energy companies have prioritised cash preservation and liquidity, and those that are overleveraged have had to take significant steps to restructure balance sheets. During the second quarter of 2020, 18 companies filed for bankruptcy, including shale producers such as Chesapeake Energy, Ultra Petroleum, Unit Corporation and Whiting Petroleum. Within the REL portfolio, significant actions have been taken to reduce costs through headcount and G&A reductions, as well as lowering capital expenditures significantly or down to zero. Riverstone also has been proactively engaging with lenders to provide additional runway as it relates to impending debt obligations where possible. Finally, to further protect against the downside, REL's E&P portfolio companies have hedged approximately 50 per cent. of forecasted oil production through year-end 2020 at a weighted average price of $42 per barrel.

Unfortunately, the current dynamics in the broader environment have translated into depressed valuations across all energy subsectors, compounding trends that have persisted since the commodity price downturn began in 2014.

Property - UK

(compare UK property funds **here**)

Mark Pain, chairman of Empiric Student Property – 15 August:

The attractive fundamentals of increasing structural demand from both domestic and international students for premium, responsibly managed student accommodation focused in high demand UK towns and cities remains strong, whilst the supply of such accommodation continues to be restricted. Combined with the company's robust balance sheet, differentiated well-located portfolio focused on premium studio-led and smaller buildings with rooms predominantly direct-let, and the benefits of our operational transformation continuing to strengthen, we see significant opportunities for the group to grow and deliver value to our stakeholders despite the short-term uncertainty.

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Manager's report for Impact Healthcare REIT – 12 August:

A number of drivers influence the demand for the care of older people.

1. Growing demand

People aged over 85 are the fastest-growing part of the UK population and make up the core client group for care homes. According to the Office for National Statistics, the number of people over 85 years old in the UK is forecast almost to double by 2043. While the impact of the COVID-19 pandemic has reduced care home occupancy in the short term, demand for elderly care is forecast to grow over the longer term.

2. Capacity is not rising in line with demand

Over the past 10 years, the number of available beds has not increased. Underlying this apparent stability there have been a number of changes in the structure of the market. Independent operators, both for profit and not for profit, have continued to take market share from homes owned and operated by the public sector. At the same time, the number of independent sector homes has shrunk by 10% over the past 10 years as older and smaller buildings are withdrawn from the market to be replaced by more modern, larger homes. The average size of an independent care home has grown from 35 beds to 42 beds in that period.

3. An increasingly fragmented market

Over recent years the market has seen deconsolidation at its top end. The market share of the 10 largest independent operators has declined from a peak of 27% in 2006 to 21% in 2019. This reflects the diseconomies of scale in the care business. For the larger operators, the potential benefits of access to capital at lower cost and purchasing power for consumables such as utilities and food tend to be more than cancelled out by higher group overheads and the lack of economies of scale in pay rates for care staff, which are operators' largest expenditure.

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Sir Richard Jewson, chairman of Tritax Big Box – 6 August:

The outlook for logistics real estate remains strong and increasingly positive. Occupational and investment demand has remained elevated with the COVID-19 pandemic appearing only to accelerate the tailwinds that have benefitted the sector in recent years. Despite these positives, it is prudent to maintain a cautious outlook on the longer-term impacts from COVID-19, particularly in the face of a potentially deep and protracted recession. We are maintaining an appropriately cautious stance in light of potential longer-term effects from COVID-19 on our customers and the wider economy.

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Will Fulton, manager of UK Commercial Property REIT – 6 August:

While it is likely that April will prove to be the nadir for the economy, the shape and speed of recovery remain uncertain at present. All told, we are forecasting a 12.9% contraction in GDP for this calendar year and then a strong, but still partial, recovery of 11.8% growth in 2021. Our house view forecast for a theoretical balanced portfolio of "All Property" expects capital values to fall by more than 14% for this calendar year, with a total return of -9.5%. This would be the second weakest nominal return in the 40-year history of MSCI data. We continue to expect retail to drag the market down, with shopping centre returns forecast to be down 31% over the year. With the segment recording a -9.1% return in the first quarter and the occupier outlook deteriorating substantially since, there may be downside risk even still.

Property - Europe

(compare European property funds here)

Jonathan Laredo, manager of Yew Grove REIT– 14 August:

2020 has been dominated by the Covid-19 pandemic. Ireland's open, outward facing economy is almost uniquely embedded in and dependent on, the health of global businesses, particularly multinationals. The attractions of a young, well-educated and highly skilled working population and an open economy situated in one of the world's largest trading blocs has over the past decade proved a huge attraction for global business. That together with IDA Ireland's focus on attracting high growth business sectors in technology, life sciences and technical engineering has helped reinvigorate the economy and been the driver of the country's success as it recovered from the global financial crisis.

Today Ireland faces the challenges of how to emerge from lockdown and how to adapt to the new normal. The effect of the virus on individuals' confidence will affect how people return to work and their daily interactions. The medium-term business outlook is also uniquely dependent on a number of interlinked geo-political, health and economic developments, none of which can be forecast with certainty. Whilst global markets appear to be recovering their poise after the second quarter convulsions that threatened the worst performance since the 1930s Great Depression, it is difficult to say with equanimity that that is also true of the underlying national or global economies. The fiscal stimuli released across the world have temporarily insulated many people from the effects of unemployment. However, as that support ends there are large swathes of the economy which depend upon individuals spending, and while that can be encouraged by governments it requires increased consumer confidence. If the health crisis is not contained, or does not reach a natural conclusion, then a second wave or uncontrolled expansion of the outbreaks (such as may have been seen in the US, Brazil and India) could trigger further negative economic consequences as those countries and populations try to deal with their health concerns. On the other hand, if the capital markets are a harbinger of economic upturn then the Irish economy should be one of the best performers, with a more rapid exit and recovery than those countries with more domestically based economies.

Savills reported that the first quarter for the Dublin office market was active, with take-up at 75% above the ten year run rate and net absorption (at 42,565 sq. metres) almost twice the ten year run rate which had resulted in vacancy falling to 8.1% from 8.6% at the end of 2019 (source: Savills Research, May 2020, 'Dublin Office Market'). As the lockdown hit, Savills estimate that of the 88,488 sq. metres of demand at the end of Q1, 15,460 sq. metres has fallen away and a further 13,730 sq. metres has been put on hold pending greater certainty on Covid-19, while the balance is proceeding and some of which has completed. However, not only did transactions continue during the second quarter but new tenant demands for space are beginning to emerge and we have seen recent evidence of multiple lettings in the North Docks, evidencing the continued health of the Dublin office market.

Outside of Dublin where the pandemic also presents health, social and economic concerns, the office market is fundamentally different (perhaps with the exception of Cork).

In Galway take-up rates were significantly constrained by the lack of suitable available space. There was less than 17,000 sq. metres of office vacancy, with only six units above 1,000 sq. metres and none above 2,000 sq. metres. Most of the limited take-up was in the better Grade A buildings. Vacancy rates across all grades and availability sits at 5.5%. The continued lack of suitable space and the strength of local business demand has launched office development, which is expected to supply c. 26,000 sq. metres, split between the city centre and suburbs which, on expected delivery in 2021/22, should help to restart the market.

In Limerick, a busy 2019 continued into the first quarter of 2020 and saw the vacancy rate fall to 10.5% from 13% a year previously, the lowest on record (source: Cushman & Wakefield 'Limerick Office Market Q1 2020'), with the net vacancy rate at 9.3%. Approximately half of the available space is Grade A, the majority of which was under discussion for occupation in March and it is expected that this net vacancy will continue to trend lower towards the end of 2020. After a flurry of development in 2018/19 there is currently no further development underway, but a number of planning applications were underway and as the city emerges from lockdown and the existing space is absorbed, it is expected that development should restart.

Cork, which was the most developed of the regional markets, saw most of its late 2019 and early 2020 take-up concentrated in the city centre. Vacancy rates across the city fell to 8.9% in Q1 2020 from 9.4% in Q4 2019 with net vacancy at 4.7% and most of the reserved space being Grade A, principally in the city centre. Speculative development continues in the city centre where only 19% of the space slated for delivery in 2021 and 2022 is reserved.

Industrial markets' activity

The industrial market across the country has, for the past few years, seen shrinking vacancy, increased take-up and rising rents. The first quarter saw take-up in the Dublin market at over 32% above the long run average with new builds accounting for 18% of that take-up. Vacancy rates in logistics remain very low at 2.6% by the end of the first quarter, speculative development is increasing, but at a slower rate than demand.

In Galway the lack of space continues to constrain activity. Total vacancy (22,950 sq. metres) stands at 4.8%, with under 8,500 sq. metres of Grade A space, only one unit above 5,000 sq. metres and only six units above 1,000 sq. metres. Despite high levels of demand for space, rental yields do not support speculative development and the only development activity has been and continues to be design and build.

Limerick saw an active quarter and vacancy levels fell to 10.3%, (91,750 sq. metres), the lowest for a number of years of which Grade A accounted for 20%. The increase in activity in 2019 and the first quarter of 2020 has triggered development, with approximately 44,740 sq. metres under construction of which 31% is speculative, principally in Shannon.

Cork also saw strong levels of take-up in the first quarter with owner occupiers leading the way. Vacancy levels (65,400 sq. metres) have fallen to 5%, a multi-year low which suggest an inflection point in the market. Development activity has been limited with some speculative development where properties have been quickly let and some design and build.

Office market outlook

Across the globe the key question facing office occupiers, especially in large cities where workers have crowded, often lengthy commutes, is how their offices will be used in the post Covid-19 environment. In Ireland, as in much of the rest of Europe, office-based employees and employers have been through an enforced experiment in working from home with meetings almost exclusively done remotely by phone or via video link. The debate about how this will impact the future of the office has begun in earnest and that future will be made manifest over the next few years; but for now a number of issues are beginning to emerge and are covered in depth by the larger property specialists.

Anything said here has to read with the caveat that any future direction will largely be driven by the course of the pandemic and whether an effective, available vaccine can be found. However, it is likely that unless that happens soon the experience will affect generational behaviour and we should expect that to change employers' office plans. Looking at some of the more obvious issues and their potential solutions it looks as if the office of the future could well look more like the office of the past with open plan layouts giving way to partitioned space, and that the principal property impact of this crisis will be on large offices in large cities.

Employee health concerns will drive change. So, for example, social distancing and sanitation will become more important, especially in multi-let buildings where there are shared facilities such as toilets or where lifts are relied on for entry or exit. Tenants are likely to want to control all facilities within their own demise, which could spell a material reduction in demand for the co-working model. Similarly, we expect that the move to increasingly air-conditioned offices will slow and potentially reverse. Given the significant expense of improving existing air conditioning systems to hospital filtration standard or negative pressure (allowing for separate areas to remain uncontaminated by recirculated airflow), it is likely that naturally ventilated spaces or air conditioning that works with natural ventilation will become more popular and be seen as preferable.

The past few years have seen occupational density increase, especially in city centre offices. Dublin was a relative latecomer to this process, but until the Covid-19 pandemic higher future densities were expected. Last year the average density per employee in Dublin was c.10.3 sq. metres and newer designs envisaged that shrinking to c.5 sq. metres. It is likely that the move back to less densely designed spaces (already seen in the US with planning for minimum densities of 10.2 to 10.4 sq. metres) will become the norm and there is likely to be less focus on, and a reversal of, open plan/shared or communal space and increased cellularisation. Dublin, unlike many other large European cities, does not have many high rise or very large office blocks, but the lack of parking facilities and the challenges of commuting may lead to some change on the future.

At least in the short term, there is likely to be a move away from the use of public transport in favour of private motor vehicles, walking or cycling to work. The lack of parking in central Dublin and the Dublin commute distances makes suburban offices (provided they have suitable parking and changing/showering facilities) more attractive for employees until increased protection or an effective vaccine gives people more confidence to return to public transport. The cost benefits in paying suburban versus city centre rents makes the attractions to employers even more transparent.

In Dublin, it looks as if the health crisis could move the office market to smaller, more manageable floorplates (allowing single tenancy occupation) and buildings with fewer floors. For Dublin city-centre offices, we expect that the best properties should fare relatively well as while there is an active Grade A development pipeline, much

of this is already spoken for. It is likely that secondary and tertiary city centre buildings will increasingly have to compete with "Core+" (Dublin 1,3,7 and 8) or suburban locations. This could reduce demand for, or rent pressure on, Core+ property which has over the past few years been the fastest growing office rental market in the country, while providing a boost for good quality, well sited, suburban business parks, especially those buildings that are accessible, modern and do not require extensive capital investment.

Several large employers have begun to explore 'hub and spoke' working patterns with a hub at a centralised head office (used by senior management or for meetings where a central location is most convenient and face to face meetings are more productive than virtual ones) and suburban spoke offices which allow staff shorter and more manageable commutes to more easily managed, cheaper buildings. It is probable that this will be a predominantly Dublin solution given the small size of the regional cities and towns where offices are often situated in the suburbs and where public transport is not extensively relied on for commuting. In most regional locations we expect that offices will be used in some sort of combination with flexible home working arrangements for those employees whose role and personal circumstances make that attractive and productive.

In the regional markets, given the lack of availability and general age of most occupied buildings we expect two principal changes. First, occupiers will look to have their buildings upgraded to make them safer and more convenient to use. This is likely to marginally increase rents, but given the capital outlays involved will probably be net neutral for owners. However, there will be ongoing demand for new space of an appropriate quality and size to suit larger tenants. For most businesses, working from home is not an alternative to the office, but if formally arranged it might reduce pressure to expand and therefore slow rental growth in what are already severely constrained markets. On balance we expect the effect to moderate the speed of rental growth rather than to soften rental levels. Given the rent required to justify development the underlying pressure is still upward. We have already seen this in Limerick as rents for Grade A property have moved above €20 psf from €19.40 psf in 2019 and could continue to rise to c. €25 psf. We expect the same effect in Galway where development is just beginning and that will slowly affect the smaller markets and IDA Ireland business parks. Cork has a large volume of mostly speculative city centre development and it remains to be seen how post Covid-19 conditions affect that city's property markets. Depending on how the Cork centre performs post-COVID-19, we expect to see a true centre/suburban market develop with Mahon Point and potentially the Airport Business Park emerging as the best suburban options and providing a cheaper alternative to the central prime offices. Rents in the city centre are currently running at c. €30 psf to €35 psf and a two-speed market will see suburban rents at between €16 psf and €22 psf.

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