Lincolnshire COUNTY COUNCIL
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Regulatory and Other Committee

Open Report on behalf of Andrew Crookham, Executive Director – Resources

Report to:	**Pensions Committee**
Date:	**19 March 2020**
Subject:	**Independent Advisor's Report**

Summary:

This report provides a market commentary by the Committee's Independent Advisor on the current state of global investment markets.

Recommendation(s):

That the Committee note the report.

Background

Investment Commentary – March 2020

How will the Coronavirus affect the health of the Global Economy?

Recent market movements

For most of February, investment markets were taking a relaxed attitude to the developing Coronavirus threat. They probably believed that either the Chinese authorities would successfully contain the threat or alternatively that any impact on the global economy would be readily offset by the Central Banks of the world.

US equities hit an all-time high in mid-February and many other equity markets were at or pretty close to their peak levels. And bond yields were flirting with previous price highs, i.e. yield lows. However, in late February, as significant cases of infection were revealed outside China, in South Korea, Italy, Iran etc, equity markets reacted sharply downwards, with falls of around 10%. And, bond yields fell once more, i.e. prices rose. It was not quite a good, old fashioned panic – but getting uncomfortably close!

Coronavirus

Medically, the Coronavirus does not appear especially potent. Certainly not compared to the usual winter strains of influenza, which is far more widespread

and has a higher mortality rate. And does not attract more than routine media headlines. The draconian, if warranted, actions of the Chinese authorities in isolating Wuhan (a city of over 10 million citizens) changed everything and was news everywhere around the world. The Coronavirus itself does not seem to be especially harmful to young people: the average age of those dying from it is in the mid 70's and often with pre-existing medical conditions.

At present, the medical authorities around the world have few specific treatments other than quarantine. And it is this that is the threat to the global economy and that has led to stock market "jitters". Before the outbreak of the virus, the growth rate of the global economy was certainly slowing down, with the US and China still expanding and Europe and Japan in the doldrums, if not actually in recession. The UK was advancing modestly. The vulnerability of the global economy stems from its interdependence on trading partners, notably China, for a complex supply chain of component parts and raw materials. Quite how this pans in the coming weeks is impossible to define. The potential for serious disruption, for example in the motor industry, is obvious and could last some months. Added to this is a sharp reduction in demand from consumers in some sectors, e.g. airline travel, leisure, and conferencing.

Trade negotiations between China and the USA

Before the outbreak of the virus, the US and China appeared to have reached some measure of agreement – the so called "phase one" agreement. Seemingly this gave the US little of what it was demanding and no doubt the fact that 2020 is the year of the election of the President and for a third of the seats in the US Senate had something to do with the pause in negotiations. So, this topic was removed, at least temporarily, from the list of professional investors' anxieties.

There are still some anxieties about the health of the US economy but employment is at record high levels and consumers are still spending fairly freely. Presidential election year traditionally sees a short term boost to economic growth but this year the saga of Boeing's 737 Max aircraft, the manufacture of which has been suspended for many months following the two disastrous crashes, has had a surprisingly large negative effect, perhaps as much as 0.25% per annum on the US GDP growth rate.

In the UK, the Brexit negotiations are likely to constrain the UK equity markets, and less so, European ones. Boris Johnson's hard line stance on the negotiations leaves open the possibility of the UK leaving without a deal. And President Macron, of France, is seemingly intransigent on a number of issues, e.g. fishing, which also raises that likelihood.

Conclusion

The Coronavirus is a "flu type" illness. So most observers expect it to recede as the weather in the northern hemisphere turns from winter into spring and then summer. That will at least bring some respite and enable time for vaccine treatments to be developed. It does not remove the threat of a return next winter.

At the time of writing, new cases of Coronavirus are falling in China (a welcome sign) but increasing elsewhere in the world. The situation remains very fluid from day to day and I expect stock markets to react accordingly.

My working assumption, at this stage, is that there will be at least one quarter when the Coronavirus, the disruption to supply chains and inadequate demand in selected sectors dominate headlines. But they will gradually return to normal and permit more orderly investment markets, which should bring renewed buoyancy in equity markets and a modest rise in bond yields.

Peter Jones

2 March 2020

Consultation

a) Have Risks and Impact Analysis been carried out?

Yes

b) Risks and Impact Analysis

The Pension Fund has a risk register which can be obtained by contacting the author of this report.

Background Papers

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