Market and Economic Review
October 2020

In hindsight, a little exuberance in share markets is easy to identify. The strong August performance of shares, particularly US technology, had all the hallmarks of a 'greed' driven rally. It's still not clear what exactly caused the turnaround, but September performance has been virtually the mirror image with broadly negative returns across share markets.

Milford's investment team recognised the increasing risks and responded in two ways. Firstly, a more cautiously invested stance was taken, with increased levels of cash or protection taken out against market falls. Secondly, there was discipline on the stock selection side where we took profits on some of our recent winners. As a result, although Fund performances in the month are negative, the Funds have managed to hold onto a large portion of the gains seen over the past few months.

The global economic recovery has been enabled by stimulus from governments and central banks, with JP Morgan estimating that fiscal support will add 3.7% to global GDP this year. The 'V' shaped recovery in consumer spending in the face of significant global unemployment is clear evidence of this policy success.

Looking ahead, the path is less clear. Consumer spending has been on goods as opposed to services, and therefore much more likely to be one-off in nature. Services spending (e.g. leisure, travel and dining) will continue to be impaired until we have a widely distributed vaccine for COVID-19. Stimulus checks from governments may be harder to come by, for example the US government has failed to agree to a renewed spending package after the previous one expired at the end of July.

Elections also loom large. In NZ, the outcome appears to be reasonably clear with the current government likely to resume power. In the US though, chances are high that they will have a change in government. Furthermore, the risk of a contested outcome is high – creating an increase in uncertainty that would surely roil global share markets.

The recent pullback in shares means we do have increased conviction in shares that can support their valuations with reasonable and sustainable dividend yields. Given the risks to the global outlook and higher valuations we remain more cautious on international shares. However, with monetary stimulus remaining supportive for asset prices, we remain largely fully invested.

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