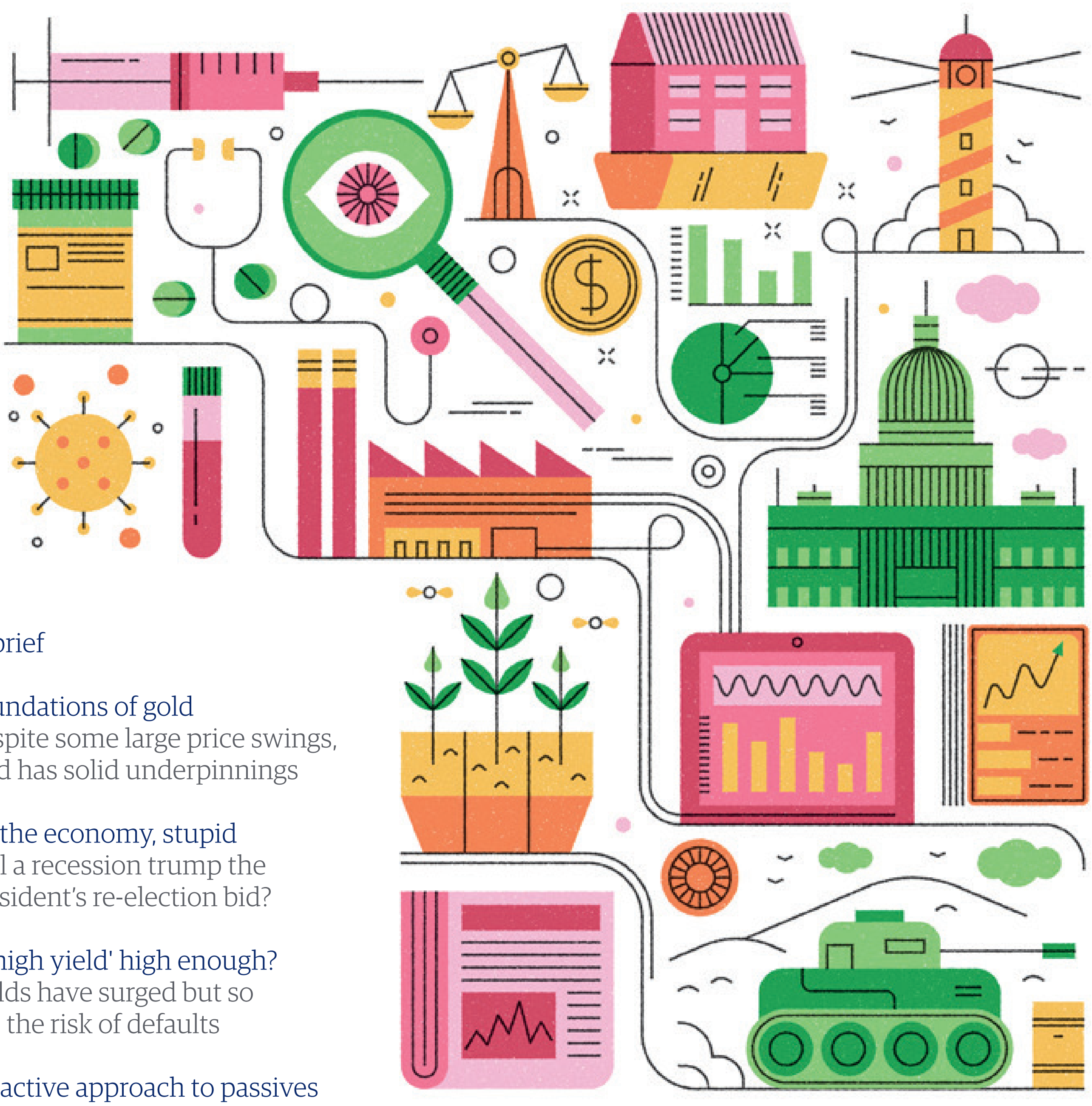
Investment*Insights*

Issue 24 — Second quarter 2020

When the going gets tough

The world economy has been turned upside down by coronavirus.
Some companies are better positioned than others to survive the crisis.



In brief

Rathbones
Look forward

Foreword

Our lives have been turned upside down by the coronavirus crisis, which is having a profound impact on the global economy and financial markets. Governments are working hard not just to slow the spread of the virus but also to help businesses and their employees. They've announced a range of extraordinary measures, which are being supported by action from central banks.

In this latest edition of Investment*Insights* we explain how the disruption caused by the pandemic is affecting the investment environment. Our lead article explores how some industries are much more likely to struggle than others — the aviation, tourism and events sectors to name a few. Yet there are certain precautions investors can take to help protect their portfolios from an uncertain future.

As investors flocked to safe havens following the COVID-19 outbreak, gold enjoyed an extra boost. Although prices were volatile following a surge in the value of the US dollar and speculation that investors were selling their safest investments, we explain why we think gold still has strong underpinnings on page 5.

History shows that the economy provides one of the most reliable predictions of US presidential elections. Putting together our own prediction model, we've determined the likelihood of Donald Trump winning a second term as US President against various economic backdrops on page 6.

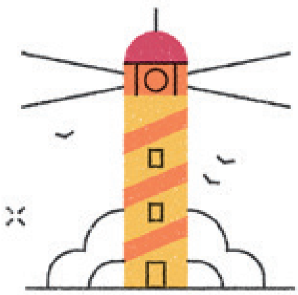
On page 8, we explore the challenges currently faced by the high yield bond market. These lower-quality bonds have been hit by market disruption caused by the pandemic, as well as the oil price war that soon followed. With default rates expected to increase, are high yield bonds worth the risk?

In our final article on page 9, we explain how passive investments can be part of an active approach to managing portfolios, and the two are not mutually exclusive. By taking into account the opportunities provided by both approaches, as well as the trade-offs between costs, asset exposure and flexibility, investors can be in a better position to reach their desired outcomes.

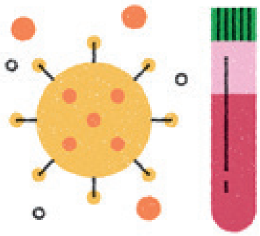
There's a lot we still don't know about the virus and what's going to happen over the weeks and months ahead. What we can say with some certainty is that life will return to normal at some point. In the meantime, please visit rathbones.com to find out more about our latest views. I hope all our clients and colleagues stay healthy and safe.

Julian

Julian Chillingworth
Chief Investment Officer



When the going gets tough



Markets have reacted to the collapse in demand that will be wrought across many sectors by attempts to contain the coronavirus outbreak, as conferences, business travel and holidays are cancelled and consumers are encouraged to stay indoors.

The longer the crisis lasts, the greater the risk that companies will face severe cash flow problems. When the economic tide is turning, as it is now, any shortcomings of business models are left exposed. As Warren Buffett famously said: "It's only when the tide goes out that you learn who's been swimming naked."

Draconian measures across the world, such as European nations quarantining entire populations, are 'black swan' events that no one could foresee. Events, tourism and aviation stocks will be especially hard hit in this slowdown due to restrictions on travel and gatherings (figure 1), showing that no two downturns are exactly alike. But there are certain precautions an investor can take to inoculate their equity portfolios against these 'unknown unknowns'.

Determining a company's defensiveness

The main aspects to focus on when assessing the defensiveness of a business are the balance sheet, the cost base and the business model.

The key measure from the balance sheet is net debt, usually defined as total debt less cash. The more indebted a business, the higher the risk that in a slump it will be unable to pay interest or refinance debt. To know whether the level of debt is appropriate, it is necessary to look at the borrowings in relation to a company's ability to pay off those debts.

A popular ratio is net debt to earnings before interest, taxes, depreciation and amortisation (EBITDA). Depreciation and amortisation are non-cash costs, so EBITDA is a reasonably good proxy for operating cash flow – but it's not perfect, as it ignores cash required for the replacement of equipment. Another commonly used yardstick is operating profit divided by interest expense, which measures how far profits would need to fall before a company defaults on its interest payments. One problem with this measure is that when interest rates are very low, even the balance sheets of highly indebted businesses can look strong. Yet any increase in rates could cause financial difficulties. That appears to be happening as coronavirus fears push corporate bond yields higher, which means companies have to pay more to borrow.

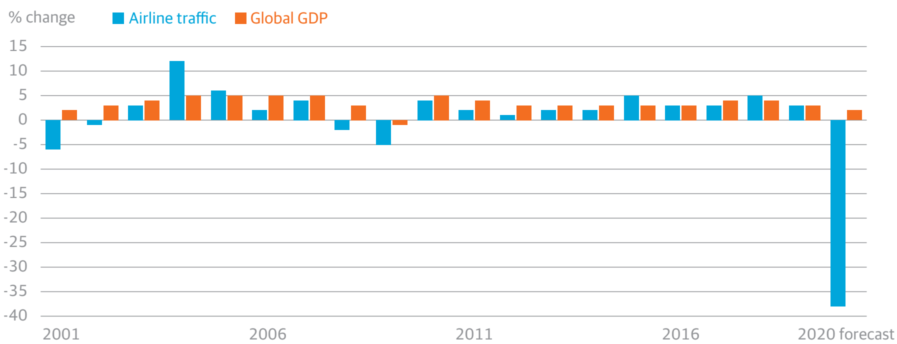
Some companies can live with higher financial gearing ratios than others. Those with reliable levels of consumption, like a water utility, can tolerate net debt of up to six times EBITDA, whereas the average for the FTSE 100 is 1.4 times. Businesses that are much more sensitive to economic ups and downs, like UK housebuilders, tend to operate with net cash. Whatever the business, investors should be aware of its debt obligations and the potential for insolvency if demand weakens.

Debt is often referred to as financial 'leverage', and it is just one of two types of leverage investors need to consider. The other is known as operational leverage – how sensitive profits are to a decline in revenues. An example of a highly leveraged business from an operational point of view is package tour operators. They pre-purchase hotel rooms up to a year in advance, and resell them at a thin mark-up, usually six to eight weeks before the date of

"It's only when the tide goes out that you learn who's been swimming naked."
Warren Buffett

Figure 1: A hard landing

The airline industry has been one of the first to suffer from the disruption caused by the coronavirus due to travel restrictions.



Source: Datastream and Rathbones.

travel, leaving them with a precarious combination of rigid costs and poor sales visibility.

By contrast, online travel agents boast beefy operating margins, take no inventory risk and have mostly variable costs, which are measured per online click. Whereas a 5% drop in revenues for a tour operator can vaporise profits, for an online agent it would barely register.

Energy and resource stocks have fixed costs of extraction that make their earnings acutely sensitive to fluctuations in commodity prices. After Saudi Arabia's recent decision to launch an oil price war, exploration stocks in the UK and US fell up to 50%. Therefore, it's important to stress-test natural resource companies to ensure that they can endure depressed commodity prices.

What's your business?

Business models are also important. For example, how easily can a company's customers cut back on its products and services? People can stop going to the cinema, put off renovating their kitchens or buying a new car, but they do need to eat, take medication, fill out their tax returns, renew their car insurance, use their debit cards, satisfy their nicotine cravings, and pay their phone subscriptions. As a result, food and beverage companies, tobacco stocks, telecommunications, accountancy, payment processors and healthcare have long been considered classic defensives.

Technology stocks are increasingly falling into the defensive bucket. Notably, the tech-heavy Nasdaq Index has outperformed the S&P 500 during the initial phase of the coronavirus. Internet platforms are hardwired into consumers' daily habits and services like social media and video on demand are either free or low cost, so their usage is relatively unaffected by a fall in spending power. Meanwhile, enterprise software vendors have shifted their business models from upfront licence sales, which can be volatile, to recurring subscription contracts.

There are also businesses that display counter-cyclical characteristics that thrive during downturns. During the current crisis, companies selling detergents, video conferencing, corporate messaging and home entertainment services like Netflix have benefited.

Unforeseen circumstances

Ideally, investors would only hold purely defensive sectors such as utilities, healthcare, telecoms and consumer staples into a recession (figure 2) and the more cyclical, or economically sensitive, ones like financials, industrials and materials into the recovery. But investors who have demonstrated such prescient timing probably owe it more to luck than skill – market bottoms and tops are notoriously difficult to predict. The father of value investing, Benjamin Graham, explained this concept by saying that in the short run, the market is like a voting machine – tallying up the preferences of market participants who are not always rational. But in the long run, the market is like a weighing machine – measuring the intrinsic worth of businesses.

Business models are important – how easily can a company's customers cut back on its products and services?

Equally, a strategy of just holding defensive sectors has its drawbacks. Every business comes with its own risks. By avoiding companies with even moderate economic sensitivity, investors would miss out on those that can outgrow their more defensive peers over the long run, have a more sustainable competitive advantage and trade on more attractive valuations.

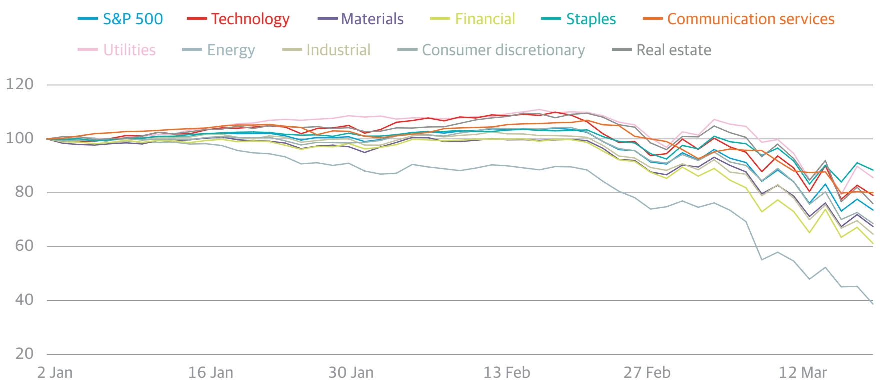
It's also important to note that recessions are infrequent and that the income lost during these periods is modest in the context of the long-term cash flow generation of a business, which is ultimately what determines intrinsic value.

Cyclicality is acceptable, providing investors don't overpay for it, there is minimal risk of breaching covenants and the company can keep generating cash even if sales drop sharply. As investors discover during every downturn, when they hold businesses with the opposite characteristics – high leverage, high fixed costs, and discretionary services – they suffer steep falls in the value of their holdings that can quickly obliterate years of previous gains.

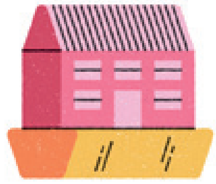
By scrutinising the balance sheet, the cost base and the nature of the business, investors can tilt their portfolios towards stocks with less earnings variability than the broader market. Such stocks can be held through thick and thin, weathering economic storms and benefiting from the upswing when it arrives. The next 12 months will be a real test of which companies are swimming naked.

Figure 2: Charting the downturn

Although all sectors in the S&P 500 Index have fallen since the start of the year, some have held up better than others.



Source: Datastream and Rathbones.
Rebased to 100 as of 2 January. Data provided for illustrative purposes only.



Despite some large price swings, gold has solid underpinnings

Gold had enjoyed a strong run even before COVID-19, and was given an extra boost when the virus spread across the world and investors headed for safe havens. Prices were volatile following a surge in the dollar and speculation that investors were selling their safest investments (figure 3). But we believe gold still has strong underpinnings, not least of which is its traditional status as a safe haven in times of turmoil.

Another trend that should work in gold's favour is negative real interest rates (meaning actual rates are below inflation). If inflation surges due to unprecedented government and central bank stimulus, that should support gold. So too should any increase in geopolitical risks, such as the oil price war deteriorating into armed conflict in the Middle East.

Gold remains resilient

Gold's brief selloff may have also been driven by a temporary rise in real rates as inflation expectations fell in the early reaction to the coronavirus outbreak. They were already very low, and fears of a deflationary bust in the global economy pushed them lower still. However, they have since stabilised, and we don't think real rates are likely to increase meaningfully in the near term. Indeed, the flood of central bank and government stimulus is also leading to some speculation that inflation could take off once recovery comes, though we also see this as unlikely given a number of structurally disinflationary trends.

If coronavirus is to be a deflationary bust, the natural hedge is usually long-dated bonds, or bonds that are more sensitive to, and therefore benefit from, falling interest rates. But in the current unusual environment of negative real yields, the cost of carry (income foregone) for holding gold is far lower than it would be normally, making it more attractive even in this scenario.

If the coronavirus crisis turns out to be a temporary demand shock, and the barrage of demand-focused monetary and fiscal stimulus then fuels rising inflation expectations, potentially pushing real yields even lower, then gold should also respond well.

One of many diversifiers

Gold is just one of many assets we classify as diversifiers – investments that tend not to move in step with equities, and which in some cases can move in the opposite direction. For diversifiers to work as part of a long-term asset allocation strategy, we believe it's important to hold a wide range of diversifying strategies and asset classes to vary exposure to different risks.

For instance, corporate bond prices fell along with shares during the 2008 financial crisis, highlighting the pitfalls of a traditional approach to diversification, which was to hold a mixture of traditional equity and fixed income securities. History has taught us that correlation across asset classes increases during periods of stress. Including a range of strategies and asset classes with a low correlation to equity markets in portfolios can help ensure better diversification.

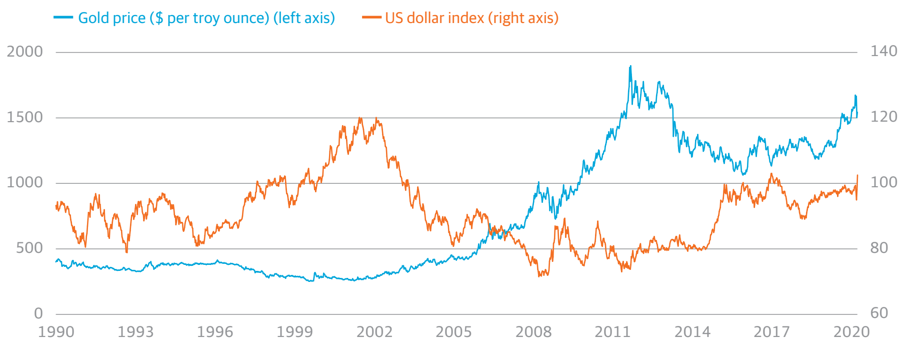
However, it still makes tactical sense to consider which diversifying strategies are most suited to the evolving investment environment. During the recent turmoil, we've seen positive returns from macroeconomic strategies, which look for relative value across different asset classes and securities.

These opportunities tend to be greater when markets are unsettled and volatility is high. Given uncertainty arising from trade wars, protectionism, US elections and now a global pandemic, we expect there will be plenty of opportunities for these strategies in the coming months.

We believe gold still has strong underpinnings, not least of which is its traditional status as a safe haven in times of turmoil.

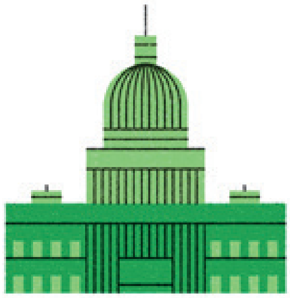
Figure 3: Gold and the US dollar

After an initial surge as the COVID-19 virus spread around the world, gold prices fell back as the value of the US dollar surged.



Source: Refinitiv and Rathbones.

Past performance is not a reliable indicator of future performance.



Will a recession trump the President's re-election bid?

Nicknamed the "Ragin' Cajun", Bill Clinton's effusive strategist James Carville hung a note on the door of his war room during the 1992 presidential election campaign that read, "The economy, stupid". Mr Clinton's campaign went on to capitalise on that year's recession, blaming it (probably unfairly) on George H W Bush's administration – and the rest is history. Mr Carville's insight has become a buzz phrase in political circles, but these are far from empty words. In fact, the economy provides the most reliable prediction of presidential elections that we have come across.

Our prediction model

With US GDP almost certain to suffer the largest quarterly contraction since 1946, where does this leave President Trump's chances of re-election? We have calculated a prediction model, indebted to the pioneering work of political scientist Ray Fair.

With the benefit of hindsight it would have successfully predicted the outcome of all 10 US presidential elections since 1980. And without the benefit of hindsight, it would have successfully predicted Donald Trump's 2016 victory that caught so many pundits by surprise.

Unlike Fair's model, we base ours on data from individual US states. In statistical jargon, our 'dependent variable' (what we're trying to explain) is the Democrats' vote share in each of the 50 states plus Washington DC. Our 'independent variables' (what we're trying to explain the vote share *with*) are state-level economic data, alongside a few other political and social variables.

Even though state-level economic data doesn't begin until the mid-1970s, our model has 510 observations (10 elections times 51 states). That makes it much more robust than a national model, which, at best, has just 25 to 30 observations even if you have the data to go back to the early 20th century.

We've experimented with a range of variables and various combinations before arriving at our baseline model. It explains the state-level vote share using:

1. The state-level rate of unemployment in the first, second and third quarters of election year.
2. The state-level growth rate of real personal income per capita in the first, second and third quarters of election year.
3. The rate of inflation during the incumbent President's term.
4. The proportion of quarters during the incumbent's administration in which state-level per capita GDP growth was above the long-run state-level trend.
5. The proportion of quarters during the incumbent's administration in which state-level per capita personal income growth was above the long-run state-level trend.
6. A dummy variable to denote if the incumbent is running again.
7. A variable to denote the number of consecutive terms in office of the incumbent party.
8. The proportion of the state identifying as (non-black) Evangelical Christian (white evangelicals overwhelmingly vote Republican).
9. 'Fixed effects' to capture state characteristics which do not vary with time (such as cultural factors).

All of these variables are highly significant in explaining voting patterns. Together they explain 83% of the variation in state votes since 1980 (which is considerable, as far as these things go). To arrive at a final forecast, we need to sum the product of the state votes multiplied by how many 'electors' each state has in the electoral college. All states apart from Maine and Nebraska operate a winner-takes-all system: the candidate who gets the largest share of the vote gets all of that state's college electors. The winning candidate needs at least 270 electors.

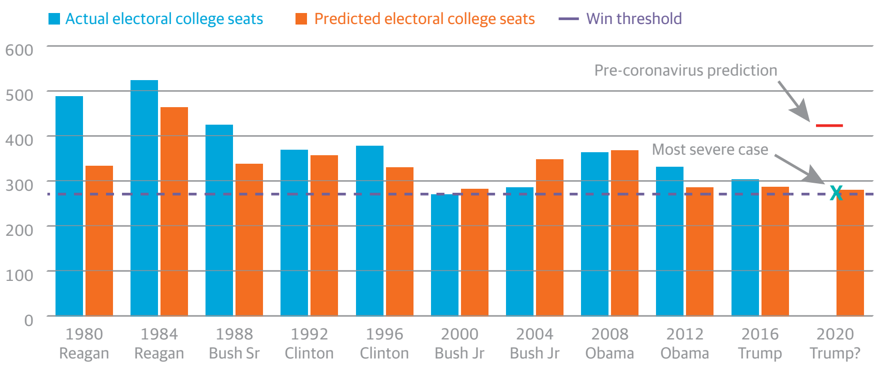
Figure 4 shows the results. Each set of bars represents the actual and predicted electoral college outcome for the winning candidates listed on the horizontal axis. The red line on the right shows that Mr Trump was on track to secure the largest victory since Mr Bush Sr if the economy had continued its recent trend up to election day.

But that's no longer possible. The orange bar and the green cross in figure 4 show the model's prediction after we make some assumptions about a virus-disrupted future. For the orange bar, our baseline, we assume that:

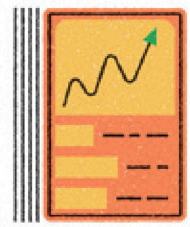
– national unemployment rises sharply to 7% in the second quarter of 2020

Figure 4: Pick a winner

Our model shows that the coronavirus crisis has reduced Donald Trump's chances of being elected for a second term, but he could still go on to win.



Source: Rathbones.



before edging back to 5.5% in the third;
– personal income contracts by 2% in the second quarter and then rises 1% in the third;
– state economies vary according to their past relationship with national economic performance; and
– GDP growth falls below trend in all states in the first three quarters of 2020.

You might think these assumptions don't square with the sharpest quarterly contraction in GDP since 1946. We believe most of the contraction will be due to the sudden pause of consumption and investment. However, we assume that the huge fiscal and monetary stimulus programme will prevent employment and incomes from contracting too sharply (in other words, the savings rate will rocket).

Trump still set to succeed

If our assumptions are correct, COVID-19 hasn't shot through Donald Trump's re-election chances. In fact, he still looks set to succeed, although his margin of victory has fallen too close to 270 for us to say that his chances are any better than 50%, given the 'standard error' of the model. The strong economy in the first three years of his term and the stimulus packages could bail out the President as well as the average homeowner.

Even in our more severe economic scenario, Mr Trump's chances are not devastated. Here we see national unemployment rise to 8.5% in the second quarter and to 9% in the third; personal income contracts by 3% in the second quarter and 0.5% in the third. Victory now looks less likely, but, again, taking into account the model's margin of error, his chances are 50:50. In other words, unemployment would need to rise above 9% and remain there (similar to the financial crisis) for President Trump's campaign to be over before it starts.

Even the best models are fallible, and we don't ever position portfolios solely on narrow quantitative signals. A blend of approaches is more robust. In an alternative model, we include the incumbent President's national approval rating. This model has more or less the same goodness of fit as our baseline, but all of our economic variables except personal income growth are rendered statistically insignificant, suggesting that historically the approval rating has been synonymous with economic performance.

We omit it from our baseline model because it would have failed to predict Mr Obama's 2012 victory, and because we lose the variation between states, which we believe is crucial. Nevertheless, the alternative model predicts similar results to our baseline – Mr Trump's approval rating has risen to a personal best.

In another alternative, we limit our sample to 18 purple states – those with a realistic chance of swinging between Democratic and Republican candidates. Most of our economic variables remain highly significant but, unsurprisingly, these states are harder to predict: the goodness of fit drops (although by less than we would have expected), and it fails to predict Mr Obama's victory in 2012. Notably, this model gives President Trump higher odds of re-election in our baseline scenario, but lower odds in our more severe scenario.

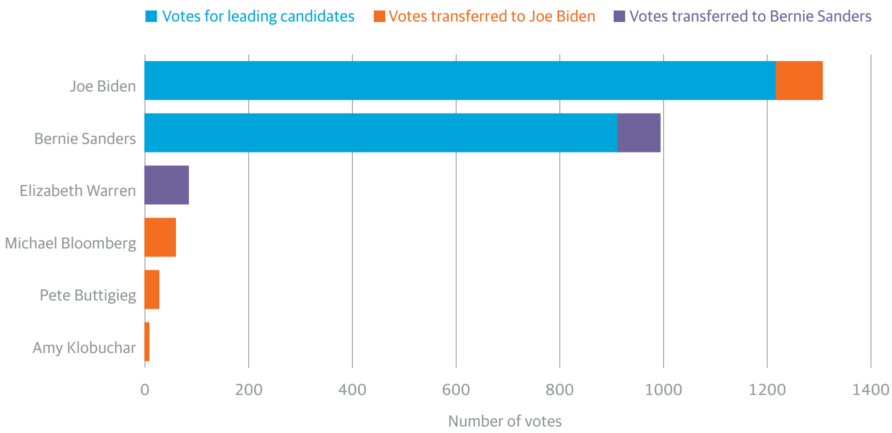
Mr Trump's opponent in November is likely to be former Vice President Joe Biden. The Democrats are two-thirds through their primary race and only two candidates remain. Mr Biden has gathered 1,215 delegates and Bernie Sanders has 910. Mr Biden needs only 46% of the remaining delegates to secure victory; Mr Sanders requires 64%, which seems well beyond reach now (figure 5).

This news should be something of a relief to investors. The Dow Jones Industrial Average has tended to do well under centrist Democratic presidents. Mr Biden would probably raise corporation tax, which decreases companies' present value, all other things equal. Yet we could argue that over the medium term, companies face a more stable future under a return to the rules-based global order, which they've profited from for so long.

The strong economy in the first three years of Mr Trump's term and the stimulus packages could bail out the President as well as the average homeowner.

Figure 5: The race for the Democratic nomination

Former Vice President Joe Biden has been building up steam and looks set to be running against Donald Trump this November.



Source: Rathbones.

Yields have surged but so has the risk of defaults

High yield bonds have been hit by a one-two punch of coronavirus-induced market disruption and the oil price war that followed in its wake. These bonds (also called junk bonds because of their low credit quality) have seen their yields, which move inversely to prices, skyrocket. So too has the spread between their yields and those of safer government bonds (figure 6), which is a measure of the extra compensation investors demand to take on the greater risk of losing their money through defaults on high yield debt.

The energy sector makes up over 10% of the US high yield bond index, and so a breakdown in talks on production cuts between OPEC and Russia (collectively known as OPEC+) exacerbated the spike in spreads. At the time of writing, they had blown out from about 4 percentage points before the COVID-19 outbreak to over 10 recently (figure 6), leaving investors to wonder whether they are now being compensated for the risk of investing in high yield bonds.

Default risk

High yield bonds are more likely to default than their investment grade counterparts with higher-quality credit ratings. Maturities are also generally significantly shorter than investment grade bonds – meaning money is being lent for a shorter period of time, reducing the likelihood of default during the life of the bond. As such, high yield issuers have to issue new bonds more frequently to refinance those that are maturing.

For the most part, this process works well – being frequent issuers in the market encourages companies to be prudent. If investors don't approve of management actions (or they have not delivered on what they promised) it will swiftly show up in the cost of capital when they try to issue their new bonds. In the worst-case scenario, not enough investors will be interested and the company will not be able to issue its bond.

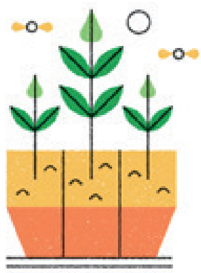
However, in the current environment when risk sentiment has nose-dived and credit spreads have widened significantly, high yield issuers are likely to find it challenging to issue bonds regardless of their performance. If they do manage to issue bonds, they will probably find interest costs are higher than they were, reducing debt affordability.

Falling revenues

At the same time that interest costs are likely to increase (or will do when an issuer comes up to the maturity of a debt facility or bond), revenue is likely to fall for the vast majority of companies as a result of the fallout from the pandemic. The impact will vary by industry sector, but only a few are likely to remain unaffected. Energy companies face another significant revenue headwind with low oil prices.

The result of all of this is likely to be rising interest costs and falling revenues for companies that are generally already running at relatively high leverage levels (hence the high yield rating). Government policy should alleviate some of this pressure, but still it seems to us that an increase in defaults is inevitable.

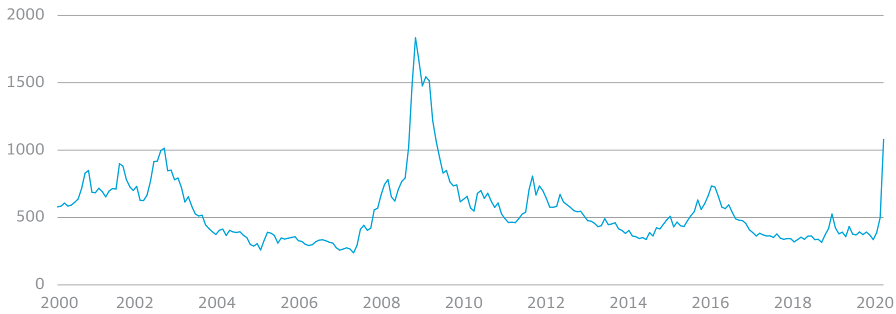
Widening credit spreads suggest markets may have already accounted for this increase in default risk. We are not convinced. At this stage, it is extremely difficult to predict how sizeable the increase in defaults could be. But with median leverage elevated compared to the past five years, it could be significant, meaning credit spreads could widen further. Considered alongside the poor liquidity we have seen in bond markets recently (meaning a position is more difficult to exit if you so desire), we believe there are better opportunities in other asset classes right now.



At this stage, it is extremely difficult to predict how sizeable the increase in defaults could be. But with borrowing elevated compared to the past five years, it could be significant.

Figure 6: US high yield bond spreads (basis points)

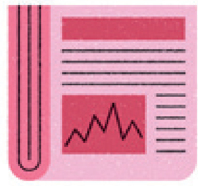
Yields relative to safe-haven Treasury bonds have surged to reflect the rising risk of high yield defaults. (100 basis points = 1 percentage point)



Source: Bloomberg and Rathbones.

Past performance is not a reliable indicator of future performance.

How to get two opposites to work together in one portfolio



It's not uncommon for an investment strategy to be followed to such an extent that it becomes almost tribal. Dedicated followers of either value or growth investing are one example. Another is the active versus passive camps, where fans of index funds argue about the virtues of simple, low-cost investing which, after fees, has outperformed many active managers.

Unlike value and growth-focused investing, which should provide contrasting exposures if executed correctly, multi-asset portfolios can benefit from holding a blend of active and passive funds. The advantages of both approaches are nuanced and the choice depends on the opportunity the market presents.

Passive funds have advantages. The biggest and almost indisputable benefit is lower cost. For instance, a FTSE 100 exchange traded fund (ETF) can cost as little as five or six basis points, while some S&P 500 ETFs are even free. They provide cheap and efficient exposure to a stock market index (also called equity beta).

Through an ETF it's also possible to gain exposure to asset classes that are difficult to buy directly, but have strong portfolio-diversifying qualities. Physically backed gold ETFs are a great example of an asset that has added a diversified source of returns to portfolios in 2020.

Far from infallible

However, when markets are particularly volatile and less liquid, ETFs can be far from infallible. Understanding these shortfalls is crucial, and can not only give active managers an edge, but also help investors make better decisions.

This situation has been more evident in 2020 with corporate bond ETFs. With more sellers than buyers during the stomach-churning falls triggered by COVID-19, and the underlying market liquidity drying up quickly, some ETFs have not only been falling in value, but at a quicker rate than the indices they are following (figure 7).

By taking into consideration various factors such as a bond's liquidity (how big the pool of buyers and sellers is), duration (a bond or portfolio's sensitivity to changes in interest rates), the underlying financial health of the issuers and portfolio cash management, active managers can have an advantage over ETFs. Lower costs are important but could prove poor value for money if an ETF is structurally flawed, or blindsided by one or more of these factors.

Under greater scrutiny

As for their equity counterparts, there are other issues to consider beyond beating an index. An income fund generally targets a yield that is greater than the market, or can grow its dividend at a greater rate. Some active managers are trying to ensure a return with a greater degree of capital preservation in down markets.

With more scrutiny on qualitative attributes such as governance and environmental considerations, these can also be factored into an active strategy. Since the start of 2020, many UK equity funds, whether open-ended or investment trusts, large or small-cap focused, income or total-return orientated, have performed well through the extraordinary turbulence on a relative and risk-adjusted basis.

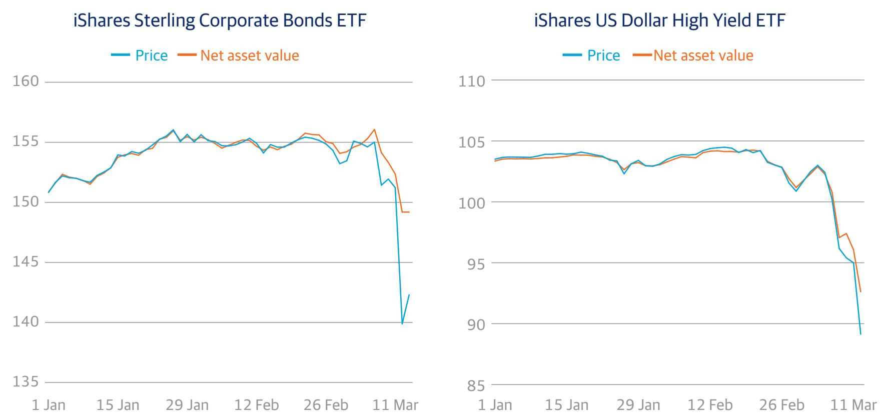
The decision to allocate to various asset classes depends on your financial objectives and goals. However, there are many advantages to building a portfolio that blends both active and passive vehicles rather than sticking with one or the other. Understanding the trade-offs between costs, asset exposure and flexibility of execution by active and passive providers can help investors reach their desired outcome.

This is the first instalment in our series of articles about passive and active investing – catch the second instalment in next quarter's Investment*Insights*.

> The advantages of active and passive approaches are nuanced and the choice depends on the opportunity the market presents.

Figure 7: A stressful performance

As liquidity has evaporated from the corporate bond markets, some ETFs have underperformed the indices they are designed to track.



Source: Bloomberg and Rathbones.
Data provided for illustrative purposes only.

Financial markets

Share prices around the world have suffered large falls over widespread expectations that coronavirus will cause a global recession, bringing the 10-year bull run to an end. From its previous peak, America's benchmark S&P 500 Index has experienced its fastest fall of more than 20% since its inception in 1957. Drops of this magnitude — signalling a bear market — have on average taken over 200 days. The speed of this fall reflects the gravity of the situation and the fact that markets have been blindsided.

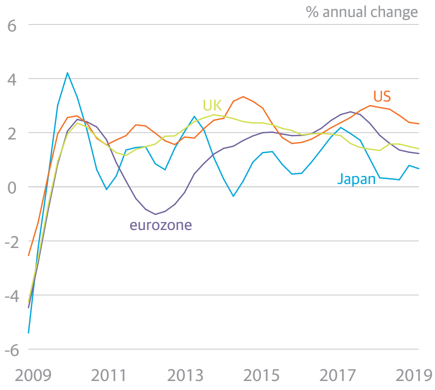
Share prices in all industry sectors have taken a hit, and the crisis is taking a particularly heavy toll on some. They include airlines, with planes grounded from the travel ban, high street shops (apart from food), restaurants and cinemas, with more than a quarter of the world's population facing restrictions about when they can leave their houses. On the other hand, companies selling detergents, video conferencing, corporate messaging and home entertainment services have benefited.

Bond yields plunge

The yields on most benchmark government bonds, including 10-year US Treasuries and UK gilts, have fallen to their lowest ever levels as investors seek a shelter from the crisis. China's $13 trillion bond market has also become an unlikely sanctuary as the price of US Treasuries rises and yields fall, increasing the attraction of higher-yielding Chinese bonds.

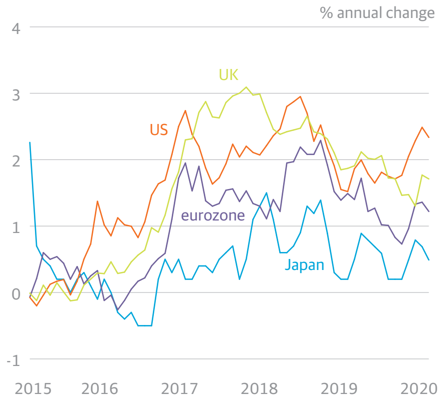
Commodity prices continued to tumble amid gloomy forecasts for industrial demand. Facing a double whammy of reduced demand and a price war started by Saudi Arabia, oil prices plunged. Gold prices, usually a haven in stressed markets, were volatile as some investors cashed in their holdings to cover losses elsewhere. Silver, which is widely used in industrial processes, was at its lowest price since 2009.

GDP growth



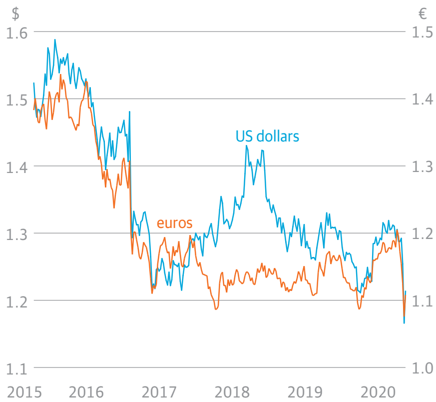
Source: Datastream and Rathbones.

Inflation



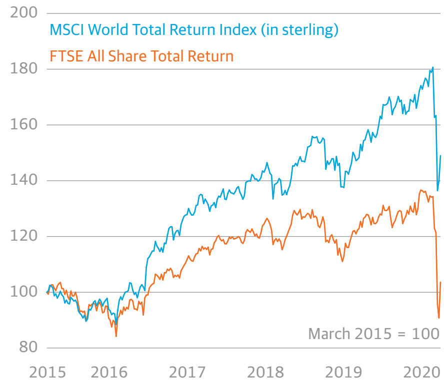
Source: Datastream and Rathbones.

Sterling



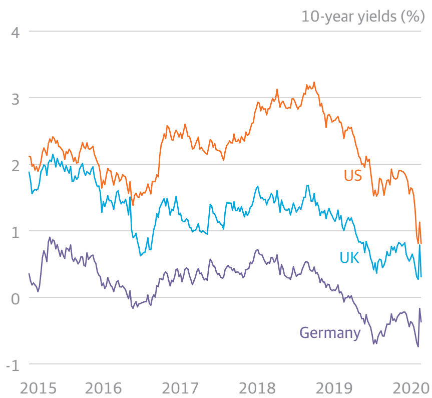
Source: Datastream and Rathbones.

Equities



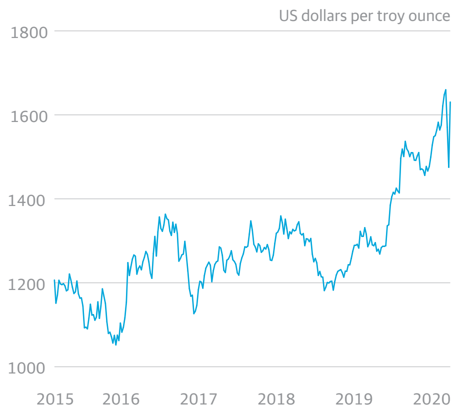
Source: Datastream and Rathbones.

Government bonds



Source: Datastream and Rathbones.

Gold



Source: Datastream and Rathbones.

Past performance is not a reliable indicator of future performance.

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**Investments can go down as well as up and you could get back less than you invested.
Past performance is not a reliable indicator of future performance.**

Taking the next step

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