
Capital Markets Outlook | First Quarter 2020 Review

 westwoodgroup.com/insight/capital-markets-outlook-1q20-review/



First Quarter 2020 Review Firm View

The first quarter of 2020 will not soon be forgotten as markets struggle to fend off viral fears.

The immediate effects of the coronavirus (COVID-19) on the global economy are becoming increasingly clear and point to a sharp fall in output across the world. Consensus forecasts see U.S. economic output (GDP) falling between 10% and 30%

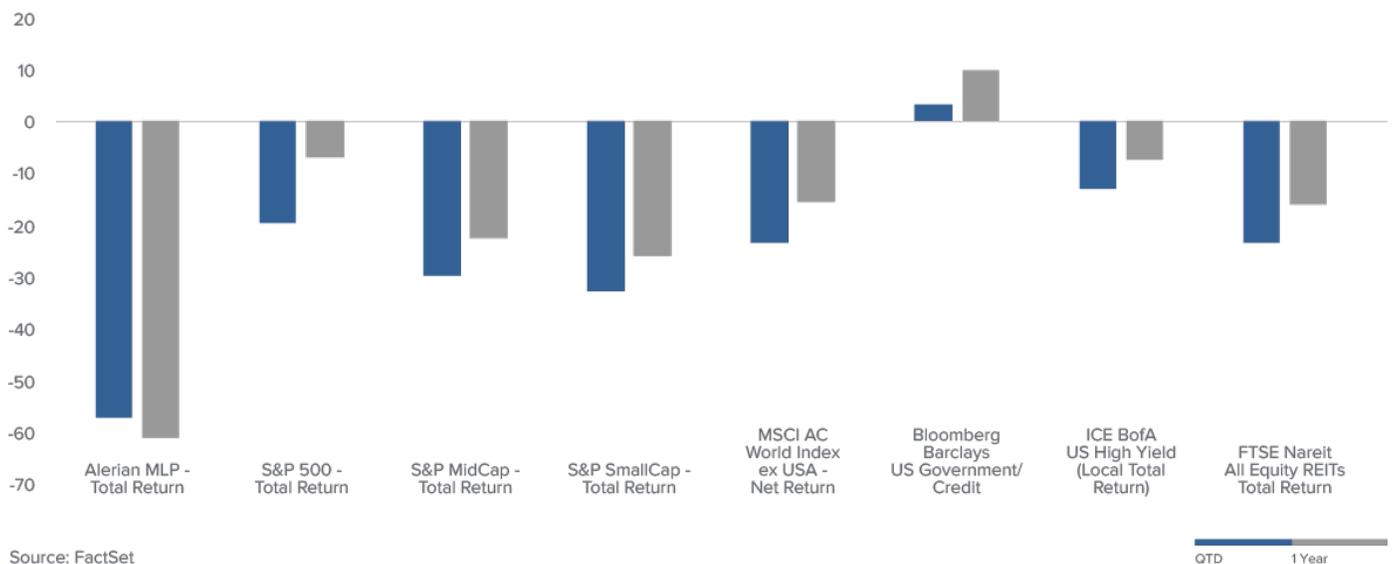
from April to June, which will drive up unemployment significantly and more rapidly than nearly any time in modern history. As a result, the world economy could contract by at least 1% this year given the constrained economic activity.

Central banks around the world have acted swiftly to support financial markets, but as history suggests, markets are only likely to bottom out when it becomes clear that the flow of new cases of the virus has peaked.

The U.S. Federal Reserve (the Fed) initiated unprecedented moves over the past month by slashing interest rates down to near 0% and through an “open-ended” expansion of the balance sheet by purchasing a range of assets. Additionally, the Fed has set up a \$300 billion facility to provide further support, with \$30 billion in losses to be backstopped by the Treasury.

With interest rates now more or less back to their effective lower bound in the U.S., Eurozone, Japan and the UK, governments are also using fiscal policy to support small businesses and individuals through various programs. On March 27, President Trump signed into law a historic \$2 trillion stimulus package, the largest emergency bailout in U.S. history, as unemployment claims surged to a record high of 22 million (as of April 16, 2020).

2020 First Quarter and One-Year Trailing Returns Across Asset Classes



Disruption in economic growth

We estimate that the increasingly stringent lockdown measures to combat COVID-19 in Europe and the U.S. are depressing the levels of consumer and business spending by more than anything we have seen since the Great Depression. The peak-to-trough decline in global and U.S. GDP is likely to be more than double that during the prolonged Global Financial Crisis.

Risk of a protracted pandemic rising

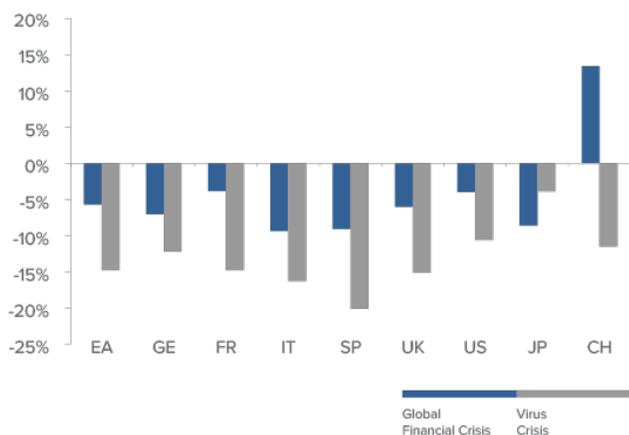
Experts indicate that the current scenario lockdown slows the growth of the virus significantly in Europe by late-April, and by early May in the U.S. The spreading virus and uneven containment raise the risk of a more protracted pandemic, with the virus persisting well into the second half of 2020 before being managed or controlled. The massive fiscal rescue packages will have to be paid for eventually.

U- or V-shape recovery?

Depending on the trajectory of the virus in each country, there is now much debate over whether a recovery will happen at a quick or slower pace. In the U.S., signs are pointing to the latter.

Commodities sold off amid global growth uncertainty, while gold rose almost 5% as a perceived safe-haven asset. Copper, steel and aluminum all suffered massive double-digit losses, but we believe that the majority of selling has occurred and a trough is forming.

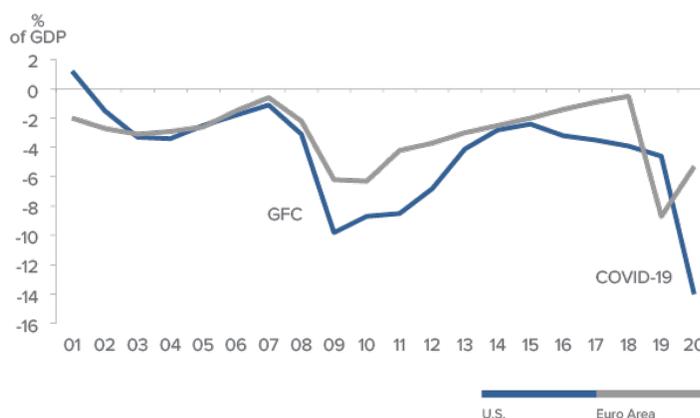
Figure 1: % GDP loss from peak to trough



Note: China "GFC Crisis" based on GDP growth over the same period the U.S. contracted; "Virus Crisis" is Q1 2020 only.

Source: Deutsche Bank Research

Figure 2: Deficit to GDP to surpass the GFC



Source: Deutsche Bank Research, Eurostat

Westwood's "20/20" Vision

As we do each year, we look ahead to 2020 and set scenarios to help guide our investment outlooks and assumptions. This provides both a time for introspective analysis for what has transpired, as well as what opportunities and pitfalls may await in the coming year. We start with our operative scenario, the most likely vision of the future, and then push our intellectual flexibility to alternative outcomes.



*For 2020, we have titled our operative scenario
“The World Has Changed.”*

The growing impact of COVID-19 around the world has led to an unprecedented contraction in economic activity and widespread uncertainty that is creating a consumption void.



The economy

GDP estimates for economies around the world have now been downgraded significantly, remaining in contraction territory for the first time since the Global Financial Crisis for at least the first half of 2020. Global central banks have provided unprecedented support, but time will tell if their measures in policy rates and asset purchases will be sufficient. Additional support from fiscal spending will also be beneficial to partially offset the slowdown in demand.



Flattening the curve

Quarantine measures and mandatory business closures, self-isolation, and increased testing, treatment and vaccination will be the key determinants of when and how conditions return to normal.



Book-ended scenarios

On both sides of the base case, there are two binary outcomes that complete the range of outcomes: 1) Programs introduced by the government may provide enough to support the consumption void, and confidence returns with higher volume of testing and slowdown in growth of cases; and 2) the overall economy fails to recover, exacerbated by lower, prolonged consumption levels and a spiraling contraction cycle. The flight to safety sends the U.S. dollar higher and populist political interests raise the risk of geopolitical flare-ups.

We remain vigilantly focused on protecting client capital during these periods of uncertainty and volatility. We strive to achieve this by investing in high-quality businesses to weather any disruptive storm.

The information contained herein represents the views of Westwood Holdings Group, Inc. at a specific point in time and is based on information believed to be reliable. No representation or warranty is made concerning the accuracy or completeness of any data compiled herein. Any statements non-factual in nature constitute only current opinion, which is subject to change. Any statements concerning financial market trends are based on current market conditions, which will fluctuate. Past performance is not indicative of future results. All information provided herein is for informational purposes only and is not intended to be, and should not be interpreted as, an offer, solicitation, or recommendation to buy or sell or otherwise invest in any of the securities/sectors/countries that may be mentioned.

The information contained herein represents the views of Westwood Holdings Group, Inc. at a specific point in time and is based on information believed to be reliable. No representation or warranty is made concerning the accuracy or completeness of any data compiled herein. Any statements non-factual in nature constitute only current opinion, which is subject to change. Any statements concerning financial market trends are based on current market conditions, which will fluctuate. Past performance is not indicative of future results. All information provided herein is for informational purposes only and is not intended to be, and should not be interpreted as, an offer, solicitation, or recommendation to buy or sell or otherwise invest in any of the securities/sectors/countries that may be mentioned.