



Capital Markets Outlook | Second Quarter 2020 Review

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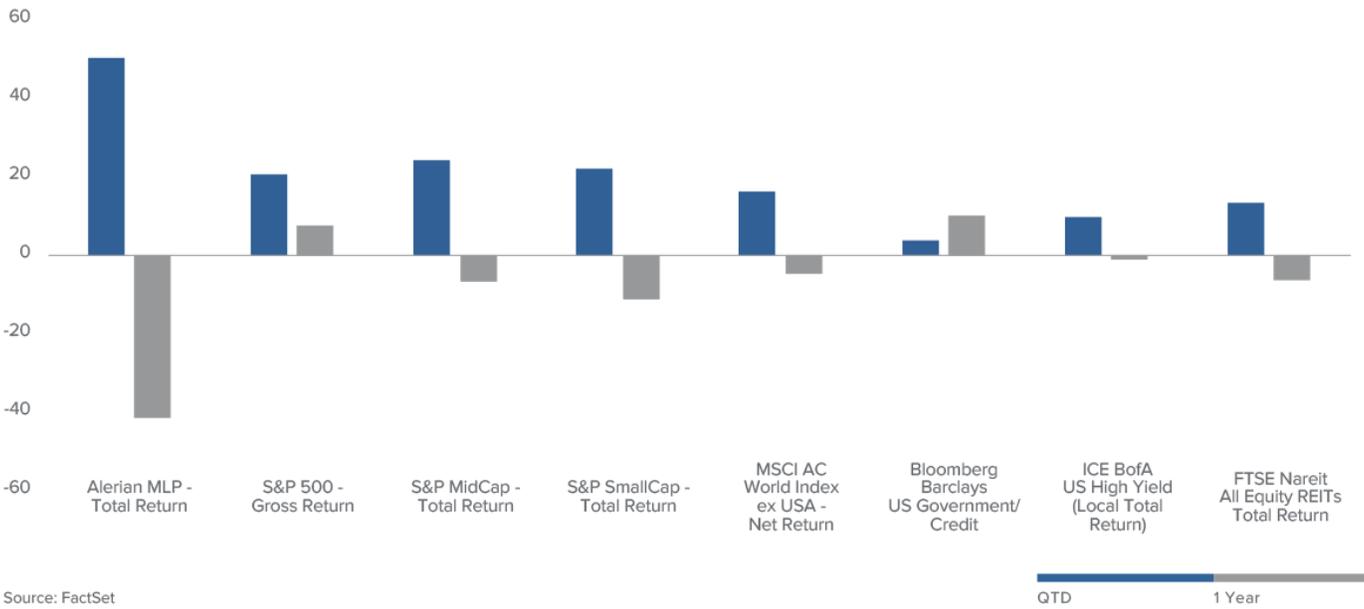
Global markets experienced a strong recovery in Q2, rebounding sharply in April with the best monthly performance since 2011, and continuing to rise in both May and June, as massive liquidity and optimistic sentiment drove investors back to risk assets. The fastest 30% drawdown was followed by the largest 50-day advance in market history in the second quarter. The S&P 500 was back above 3,100 on June 3 and the Nasdaq hit a record high on June 10.

Record levels of fiscal stimulus, sustained low interest rates and ongoing low inflation create a supportive environment for risk-asset outperformance. A gradual easing of lockdowns and resumption in economic activity in many countries took effect as positive economic surprises

drove indicators higher, including the U.S. ISM Manufacturing PMI, while copper prices, a barometer of global growth, rose 12% to within 5% of YTD highs. The green shoots of recovery sent commodities such as Brent crude oil, aluminum and silver rallying, as gold continued to outperform.

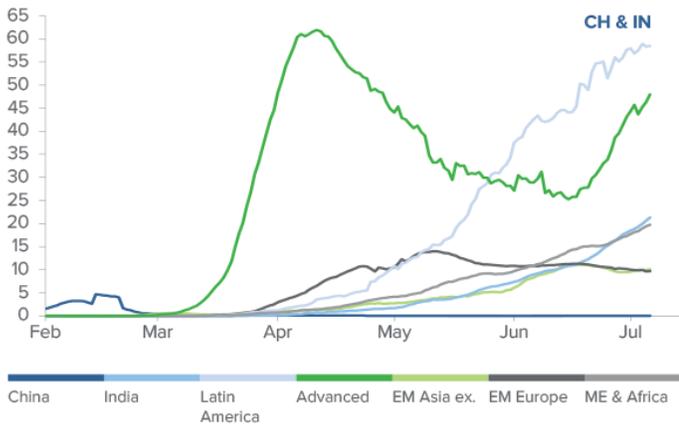
The market resurgence was tempered, however, by a selloff at the end of the period due to a new outbreak of COVID-19 cases in the U.S. and a persistent rise in number of cases in Brazil and India. The question now remains how likely a second wave attack will occur, and how long lockdowns will continue. These will have important implications for near-term market valuations.

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



Source: FactSet

Figure 1: Breakdown of New Confirmed Infections



Sources: Refinitiv, Oxford University, CEIC, Johns Hopkins, CE

Figure 2: Total Confirmed Infections

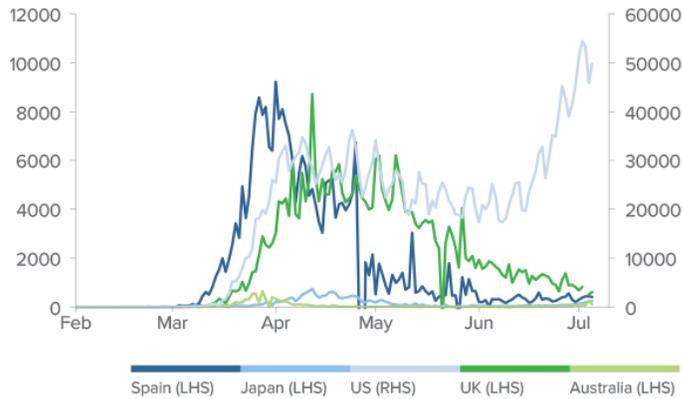
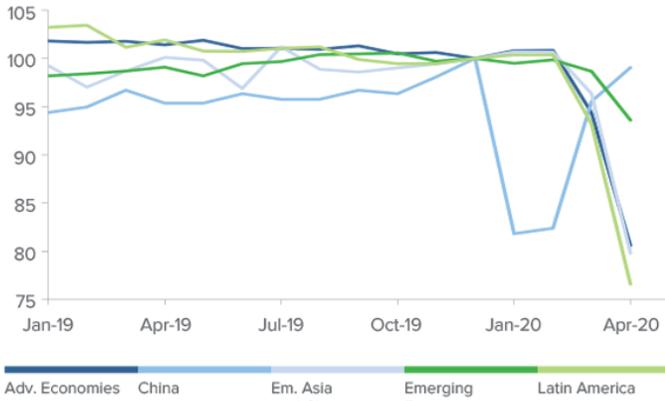
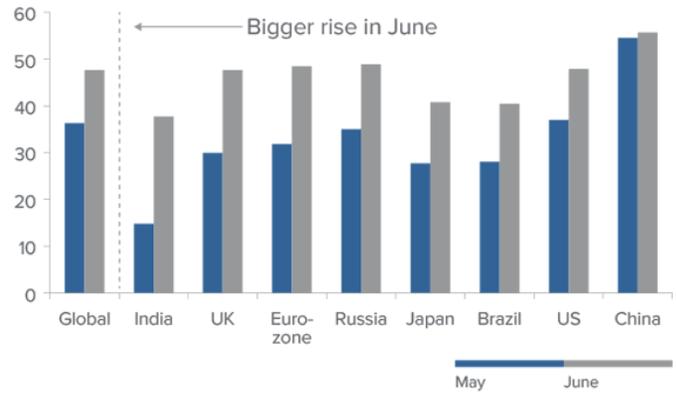


Figure 3: CPB Industrial Production (Dec-19 = 100)



Sources: Refinitiv, Oxford University, CEIC, Johns Hopkins, CE

Figure 4: Composite PMI Country Breakdown



Sources: IHS Markit, Refinitiv, Capital Economics

Market Outlook

As we do each year, we look forward into 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. Here’s what we do know:



*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. 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. On the flipside, 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.

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