A NEW NORMAL

Navigating through an evolving financial landscape during a pandemic

tam ASSET MANAGEMENT INTERNATIONAL

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WELCOME

Welcome to our complete investment guide to helping you and your clients navigate through an evolving financial landscape during a pandemic.

The coronavirus continues to affect our day-to-day lives and we want to share the ways in which we are adapting to this new reality in order to protect clients' assets, and our strategy for taking advantage of the inevitable market recovery.

Our investment management and operations teams have decades of industry experience, having survived a number of market falls in their lifetime. This has provided them with the depth of knowledge and understanding to manage different market cycles and conditions, and they have come together to share extracts of valuable industry tips and information that they have learnt, and continue to learn during the most recent COVID-19 crisis.

In addition to this guide we've launched TAM Talks - our brand new webinar series that enables us to virtually interact with you, keeping you updated with how our investment team is reacting to the current market conditions in order to protect clients' assets. We've also given our website a little facelift, complete with embedded search functionality that makes it even easier for you to find the information you need, and access all available resources quickly and simply.

We truly understand how difficult it can be coming to terms with a new normal, but hope that this guide proves a valuable resource in providing you with a positive approach to navigating your way through these unprecedented times.

Stay safe one and all, and if you ever need to speak to us then do not hesitate to get in touch, all of our contact details are below.

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Long-term market investment: Does timing count?

Looking beyond the COVID-19 crisis at the longer term it's clear we are going to be entering a new era of corporate growth and corporate flexibility. These new dynamics have the potential to topple today's corporate giants and crown new market leaders. The term "Fallen Angel" has gained notoriety.

Whilst this might be a daunting prospect, there remains one constant in investment theory which looks through the uncertainties stemming from the COVID-19 shake out. Quality will always be quality.

Robust corporate earnings, low levels of debt, high barriers to competition, cash on the balance sheet allocated responsibly for long-term growth will always be metrics that produce long-term out-performance. This new world also supports companies placing increasingly high levels of emphasis on the Environmental, Social and Governance elements of their business and the new norm is attracting positive long term interest in the company and the stock price.

The current discount from the COVID-19 sell off is an opportunity to buy investment funds which seek to own companies with these ultra-high quality credentials. Indeed, this view only gets stronger if the market sells off further from here.

> *One constant remains, **quality** will always be **quality**.*

Not panicking and focusing on the long-term advantages of buying in at these levels has to remain central to an investment strategy navigating these uncertain times. How do you do that? We are urged not to try and be bottom hunters... trying to buy at the bottom of the market doesn't work.

Income funds: A new era

Income funds have not coped well with COVID-19. A stalwart of the 80's and 90s portfolio strategy, they represent an investment vehicle seeking to pay cash out to investors from dividend payments received from UK corporates either at regular intervals during the course of a financial year or in one single payment. Since the outset of COVID-19 these funds have suffered a terrifying double headwind. Firstly the collapse in prices wiped some 20% off global stock market values. Secondly, from a sector perspective, the pandemic forced many companies to halt paying dividends, in favour of putting this capital back into their business to enable them to survive the economic shutdown. The entire raison d'être of the Income fund has a gun to its head.

As we write, over 150 FTSE All Share companies have cancelled or deferred their dividends. This represents 24% of the total UK stock market. Travel and Leisure has understandably seen the most drastic impact with the Support Service sector, House builders and Banks also seeing large cuts to their dividends. Looking to the end of the year, analysts are calculating the UK's dividend pay-out yield to be less than 3% against the long run average of 5.63%.

The double headwinds have meant income sector investors in these funds have seen the most selling pressure. Why hold an income fund that doesn't pay an income? Investors have fled these stocks on fears that these companies will no longer be able to pay a dividend, one of the primary reasons they were purchased in the first place, or possibly even survive.

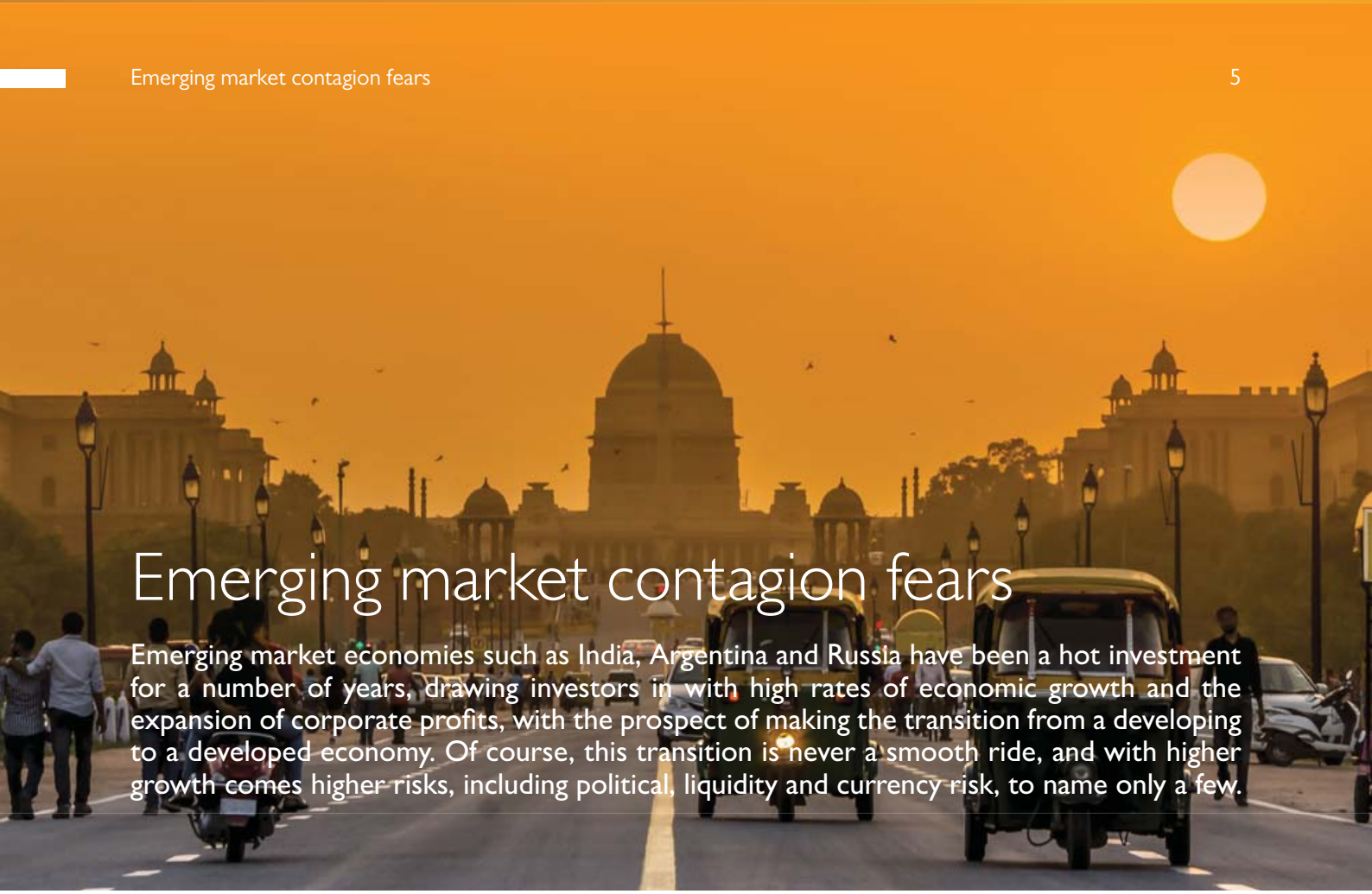
Looking forward we see real value in this sector for those with the patience to see the current uncertainty through. Why? Because, at the end of the day, a company not paying its dividend to ensure its survival has the potential to recover faster once we see a pickup in business activity. It is more akin to a dividend holiday taken whilst the company shores up its balance sheet to survive the current lockdown.

A recovery for income stocks is likely when dividends start being paid out again. That's when one can expect to see a pickup of investors, seeking dividend income, moving back into the asset class.

UK's dividend pay-out yield to be less than 3.00% against the long run average of 5.63%.

To summarise, the dividend paying sector of the stock market is a pariah at the moment. It is currently being treated like its component companies are never going to pay a dividend again! This is highly unlikely and in reality the best of these companies should resume paying a dividend as and when growth recovers in the global market place.

It's a painful place to have been invested and dividend support... has actually been no such thing.



Emerging market contagion fears

Emerging market economies such as India, Argentina and Russia have been a hot investment for a number of years, drawing investors in with high rates of economic growth and the expansion of corporate profits, with the prospect of making the transition from a developing to a developed economy. Of course, this transition is never a smooth ride, and with higher growth comes higher risks, including political, liquidity and currency risk, to name only a few.

So while these may be some of the most exciting economies from an investment perspective, they are also some of the most fragile. Throw a global health pandemic which has caused large scale disruption to global supply chains and businesses across the world at them, and you are almost certain to see cracks begin to appear in the delicate infrastructure holding them together.

Emerging market economies fared slightly better than expected during the turbulence of Q1, showing outperformance versus US, European and UK indices. Over the quarter, the MSCI Emerging Market (EM) index lost around 19.0% versus the S&P 500 index which lost 19.7%, the MSCI Europe index which lost 21.9% and the FTSE All Share index which lost roughly 25.1%. This is despite the large scale outflow from risk assets over the quarter.

While this is positive for the asset class, our fear is that the virus is yet to arrive at full strength in many of the emerging market countries, particularly the countries in Latin America. The pandemic will be a huge test of weak public health care systems and will put an increased strain on a population surviving on low wages and a limited social safety net. With governments needing to provide some form of relief effort, further pressure will be put on public finances and we may see several countries defaulting on their debt obligations. The IMF is already stepping in to avoid contagion.

Perhaps the more significant risk to the future of emerging markets is that the crisis tips the world economy into a full blown and lengthy recession. This would undoubtedly impact the emerging economies hard. Fundamentals have, for now, taken a backseat which is why we have seen indiscriminate selling across all emerging market countries.

However, once the spread of the virus has been contained and the global recovery is visible then an emerging markets rally could be sharp in nature. Although we don't know when this will be, what we do know is that selectiveness within this asset class will become more important than ever if you want to avoid the more fragile countries with shakier finances. This highlights the importance of a quality fund managers who know the market well and have a proven track record of strong stock selection within the region. TAM will continue to make it a priority to conduct thorough research and analysis to find these high quality managers, so that we can maintain well-diversified portfolios for our clients. In the meantime until contagion is contained... the jury is out.

Infrastructure investments: One way out of a hole is to dig one!

Infrastructure investments may perhaps be most directly impacted by the spread of the coronavirus and the resulting global lockdown measures. Traditional infrastructure assets, including railways, airports and toll roads, faced dramatic business declines as people were confined to their homes, while energy infrastructure also came under pressure as negative sentiment regarding the underlying commodity price filtered through the supply chain.

Having said this, the increasingly diversified nature of the asset class, which has moved away from focusing just on traditional forms of infrastructure investment may yet prove to be a silver lining for investors as some elements were able to protect capital on the downside. More importantly they could also be well-positioned to benefit from the next stages in this pandemic.

Digital infrastructure, which was already an area of interest to investors as we make the move into an increasingly digitalised society, has thrived during this period. The importance of good communication systems for people working remotely from home has become paramount, while the demand for video conferencing, HD streaming and gaming, has risen dramatically as society adjusts to the 'new normal'.

Social infrastructure, which covers healthcare, education and security, is another area that was seeing increased investment pre-coronavirus and is likely to see an acceleration afterwards. A spotlight has been shone on the healthcare systems of countries worldwide, which is likely to uncover areas where investment is needed to ensure they are fit for purpose. Public investment alone may not be enough to meet these requirements. Furthermore, increased digitalisation will only serve to heighten the need for robust cyber security systems to prevent hacking and data fraud.

Although people will begin to fly, take trains and drive their cars once again, it could be a slow process back into 'normal' life, and this could see traditional existing infrastructure companies on the back foot for some time. This will mean the less well-known areas within infrastructure investing will need to take the baton and lead the way for returns for this asset class going forward. Government expenditure which so far has been aimed at protecting against economic decline will need to become expansionist in an effort to reignite the economy. Build bridges, renew roads, improve infrastructure... and drive the economy.

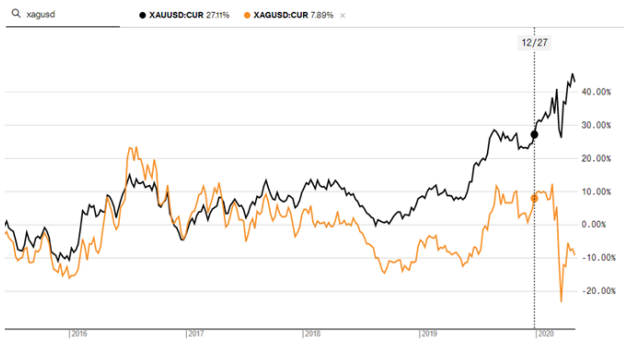
So while it was perhaps the asset class that was the hardest hit by the pandemic, it could be the one which paves the way for the economic recovery post-COVID-19. It really could be that one way out of a hole... is actually to dig one!

All that glitters is not gold, it could be silver

Unbelievably, gold was brought to us by the collapse of super nova falling to earth as cosmic dust. All true. So where does gold derive its true value?

In modern investing the value of gold is more often than not based on investor fear of the falls of other asset classes or fears of inflation.

Gold had been rising for a year or more but when global lockdowns started all was well. Then in mid-March, there was a "dash for cash", selling off pretty much any liquid asset. Gold included. A sell-off during market scares is nothing new but gold is usually the haven that investors flock to amid extreme equity volatility. This time it failed, but not for long. Gold climbed from its lows in mid-March back above the $1700 level in early May.



Source: Bloomberg

Silver has always had a strong relationship with gold but this was broken earlier this year with an unprecedented sell off to 2009 lows.

Now that investors have started to settle after the recent high volatility, precious metals have regained their poise as a "safe haven". While markets may still not have bottomed out and the risk for further disruption in traditional asset classes is significant, we are confident precious metals will provide some hedge against this volatility. Volatility, a second wave of infection or worse numbers than anticipated could see a further fall in traditional markets pushing up the relative safety of precious metals.

As we all know markets can be driven by fear into negative spirals, helped by the media with plenty of bad news to report - weakening investor confidence more than ever. This means havens such as gold and silver could see a rise in demand similar to those of 2011.

In these unprecedented times gold and silver are highly likely to maintain security value, possibly all the way up to and above $1,800? Will it make a third more historic resurgence above $2,000 an ounce? Unlikely, but possible.

The disconnect between gold and silver as seen in the chart above is not likely to last for long, notwithstanding the core argument that silver is economically driven and not as such a precious metal. Both gold and silver look likely to support portfolios in the coming months.

Property funds: Illiquidity in bricks and mortar

In the past 12 years since the financial crisis of 2008, property funds have periodically created periods of illiquidity for investors. Property funds create a solid aura of stability and consistency but they do not always live up to the billing.

The underlying investment itself is of course sound but place an illiquid asset class into a daily traded environment – such as a unitised fund – and it's a recipe for illiquidity. The FCA itself in 2018-2019 forced property funds to be more cognisant of the risks in liquidity, demanding stronger risk warnings be placed over holding such investments. Clients needed to be warned of both the higher likelihood of illiquidity and indeed the higher risk. The FCA also announced that property fund managers have the freedom to act at will, in any form of liquidity event, to close their products... 'Gate early' was the message. This was, of course, a sensible call to protect investors from the forced sales of assets.

Two things have often gone unnoticed: One is "swing/bid pricing". In periods of stress funds can divert to bid pricing, often meaning a fall in price of some 3-5%, to protect holders from fast sellers. The second is that International Life related Bonds, to all intents and purposes, have banned them! Why? Liquidity.

Twice in the period from 2008 to 2019 property funds "gated". This left investors unsure as to when and how they could redeem their investments. They eventually reopened. It's happened again almost right across the board as a result of COVID-19, but this time is different! This time the likely lock period is going to be a year and possibly even several years depending on the outcome of the pandemic. For those with the stomach for illiquidity over long periods and belief in the long-term returns for the asset class... that's no issue. For those that merely used it as a defensive diversifier in a portfolio, COVID-19 has changed the way they should use illiquid investments as diversifiers.

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Who needs oil?

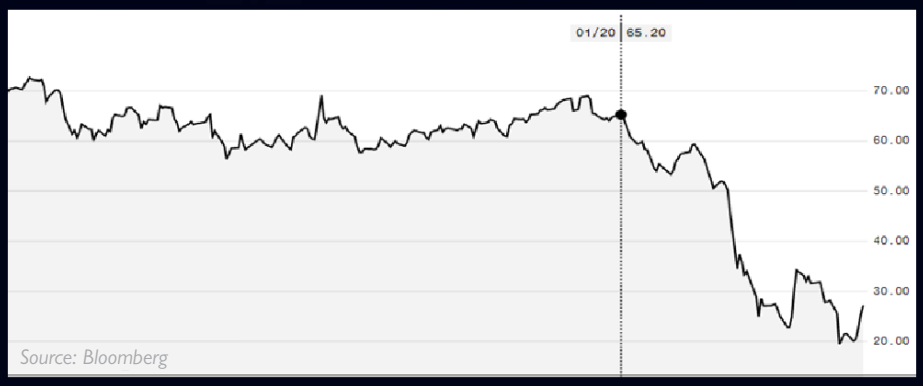
Whether you like it or not, oil is still one of the most important commodities in the world. Oil still fuels the world, transport around the world, whilst changing, is still feeding the arteries of the economy and... the supermarket shelves. Its by-products create multiple items essential to modern day life, whether it be a lifesaving ventilator or work essential computers. We need oil.

From Oil at $147 a barrel in July 2008 we hit the headlines of below zero or negative in April 2020... how did that happen? And what does it mean? The first thing is that it wasn't actually zero and Brent Crude for future delivery traded around the $25 mark and above. The headline of a negative oil price came about because no one wanted to take up/take delivery of short-term contracts of oil as it was cheaper to pay to keep it away from storage? Whoever is left holding the contract when the contract expires has to take delivery of the actual physical oil. Most who trade oil have never, and will never, see a barrel of oil, let alone take delivery of one. So the Zero headline was just a little misleading short-term delivery was significantly lower than the long-term price for sure... "a super contango".

How much a country spends on producing oil also dictates its vulnerability. Saudi Arabia has one of the lowest bills for extracting oil - but its dependence on the commodity means it too could face a funding shortfall of over $100bn. It's still recovering from the last major drop in oil prices in 2014. Attempts to push into areas such as tourism have been insufficient to plug the gap. Ironically, it was Saudi that accelerated the oil price volatility by threatening to boost production to punish its rival Russia - a country which is far less vulnerable to swings in the price of crude.

Where do we go from here? For the last year oil has been floating between $60 and $70 a barrel (Brent) then the price started to dip mid-January when the market started to see that COVID-19 might be a global issue.

Like many markets we are starting to see a pickup in confidence. Is $20 the bottom for oil? As people go back to work and start travelling again, market confidence in the need for oil will increase, China being the initial low price beneficiary.



The demand is largely dictated by government policy, some countries will open quicker than others and we do not know if there will be a resurgence once the population starts to re- integrate, so the timeline could be very blurred.

A few other things have been happening;

- Shell cuts its dividend for first time since WW2
- BP profits dived 66% as coronavirus hit oil demand and could go lower
- Very Large Crude Carrier ship rates have exploded upwards as oil is stored at sea and not in land storage capacity.

There is new history being made in the oil market. Opec producers and allies have agreed a record oil deal that will cut global output by 10% after a slump in demand caused by coronavirus lockdowns.

Will it fully recover? That is a hard one to answer. One thing that COVID-19 has done, it has made people aware of the damage we do to the planet. Indians can see the Himalayas, Venetians can see fish in their canals and the French are seeing wild boar in the streets.

Oil is unlikely to ever recover to over $100 a barrel, as transport methods become more efficient and less reliant on oil, alternative energy sources are utilised and economies become more efficient and more "green". Never say never, however.

The dash for cash: Sometimes diversification just does not help

The recent market sell-off saw indiscriminate selling in March across all asset classes, which plummeted in value simultaneously at their fastest pace in history, dashing the hopes of investors who had trusted in the much-loved theory of portfolio diversification.

While investors cannot be expected to predict the exact behaviour of an asset class and while it is not uncommon for correlations to converge during periods of market stress, the extent of this convergence was one that no investor anticipated. Perhaps the most basic relationship is the negative correlation between stocks and bonds, i.e. when equities are rising, bonds are falling and vice versa. This is the foundation on which most portfolios are constructed, with the idea that a portfolio can benefit from a rising equity market, whilst maintaining adequate protection generically from bonds. That failed in March 2020. Cautious investments capitulated along with equities.

In March alone we saw the MSCI World index fall roughly 10.9% in sterling terms, while the Barclays Global Aggregate Corporate Bond index fell alongside it, in the region of around 4.4%, with some high yield bonds suffering catastrophic falls. Often bond portfolios had gravitated to the high yield end to eke out investment return. I mean a bond is cautious isn't it? That decision came back to haunt investors. It became a case of owning assets that would fall relatively less, rather than owning the assets you believed would protect capital or even rise in value during times of stress.

Other assets typically seen as havens in times of market volatility, such as gold, also tumbled alongside riskier assets, while there was also, unbelievably, selling in the government debt market. This later coined the term "dash for cash", as investors sold any asset they could in favour of cash. It was almost unprecedented.

MARCH 2020

MSCI

-10.9%

MSCI WORLD INDEX

BARCLAYS

-4.4%

BARCLAYS GLOBAL AGGREGATE CORPORATE BOND INDEX

We must remember that no one market "crash" is the same as another and the specific combination of factors driving this one are unlikely to be replicated. There are still considerable benefits to be had in a well-diversified portfolio, but maybe it is now time to look beyond a traditional equity versus fixed income split, and more towards diversifying within asset classes by style, market capitalisation, investment theme and ESG-focused strategies.

The investment universe is more vibrant and dynamic than ever, so creating a well-balanced portfolio with exposure to exciting and innovative products taking advantage of future trends in the market, we believe, is key to delivering sustainable returns whilst protecting capital over the various market environments we will be faced with in the future.

Let's print money and buy our way out of this!

Across almost all developed economies the present crisis has seen governments on a spending spree to pick up the tab for the economic shutdown, protect workers, save companies and keep economies from the brink. This came in the form of billions in loans advanced to small businesses and further billions in payments to employees who have lost their jobs, or been furloughed in the UK, as a result of COVID-19 shutdown. The goal is simple – prop up the economy until we can get back to normal.

The need for such drastic action was learnt the hard way from the 2008 financial crisis where the US government was shown to have exacerbated the economic shock arising from the banking crisis by not releasing stimulus measures early enough. This is something they have remedied this time around, aiming to normalise the economy as quickly as possible. The question is - when do we get back to normal, and what will normal look like?

By the end of this year the US debt to GDP will hit 101% with 2021 likely pushing this to 108% as the US government rolls out a further trillion dollar economic stimulus package aimed at corporate bailouts and infrastructure projects as the economy struggles to get back to pre-COVID-19 growth.

Governments will have to issue huge levels of debt to pay for these spending measures and the central banks will be the ones buying a lot of it. History has shown us that issuing large amounts of government debt and injecting cash into markets to buy it can lead to unchecked inflation. As we speak that is a distant, but plausible prospect, but one that is almost "pre-packed".

If you increase the amount of money in the system but keep the level of goods the same, then the goods cost more to acquire, leading to price inflation. Inflation eventually risks derailing an already fragile economy and an even more fragile consumer whose disposable income remains uncertain. Furthermore, governments will have to increase their income - which inevitably means higher corporation and personal tax. Austerity measures over the longer-term will also follow as you cannot prop up economies with a cash splurge without it being repaid.

Governments don't go bust, they issue more paper and kick the can down the road. Local governments may also do so, and this is already mooted.

An asset class which indirectly benefits from rising inflation, fiscal and monetary stimulus and a crisis generally, is precious metals such as gold and silver. Both of these metals are considered real assets whose pricing is not correlated to stock and debt markets. As we know, gold was the original global currency. When markets begin to worry about an oversupply of money and the risk of inflation, investors flock to precious metals for safety.

Risk and volatility can't be avoided

Volatility and risk remain closely linked. Higher levels of both risk and volatility are evident in the current COVID-19 induced market. Breaking through the jargon - the volatility of any product (not just stocks) is the price paid for it and how much this price changes over time.

If a product's price remains very stable then the volatility is low, if a product's price changes frequently then the volatility is high. Investing in a product with a volatile price which puts your capital at risk of sharp changes in overall value can be put simplistically as taking on "risk".

The goal of investment, its nirvana, is to maintain the right level of volatility or risk within a client's investment portfolio to ensure that their investment portfolios are suited to both their goals and their tolerance for capital loss. One day may be completely different from another and this is very much why history can be no guide to the future.

Obviously with stock prices moving wildly as the COVID-19 outbreak spread into mainstream markets this caused a massive spike in volatility in all asset classes in March as investors wanted to liquidate their investments.

Volatility continued in April as investors started buying them all back again as the market rallied.

Just because the price is going up doesn't mean it's not volatile. It's the price fluctuation that has increased the overall risk levels across all asset classes, benchmarks and portfolios. Whilst this price fluctuation is understood, monitoring total risk remains paramount to controlling portfolios and the level of loss in those portfolios. Risk should remain firmly in line with investment commitments to clients.

TAM's investment team takes a cautious approach to risk and produces portfolios with volatility below that of the wider market and our benchmark. This low risk approach gives our portfolios that all important ability to defend client capital in times of increased risk. The proof of the pudding is in the investment return.

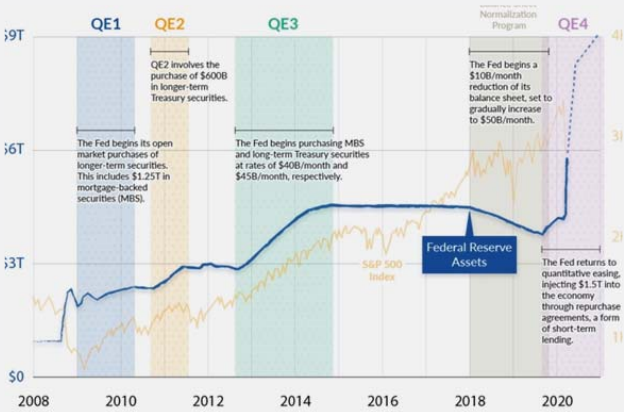
Quantitative easing: Will it ever stop?

With coronavirus lockdown wreaking economic havoc, governments and central banks around the world have been quick to react by introducing schemes to support employees, employers and companies in the worst hit industries.

In the UK, the government pledged to support 'furloughed' workers, subsidising their salary by 80% (up to £2,500 a month) and offered a number of incentives for businesses, including government -backed loans, grants and tax deferral. Over fifty percent of British adults are now receiving money from the state in one form or another.

In Europe, EU fiscal rules have been relaxed to provide member states with maximum flexibility so they can act decisively. Collectively, fiscal support measures now account for 2.2% of total EU GDP. However, member states have failed to present a unified front, delaying further EU packages which would increase their total fiscal response to the epidemic to €3.2 trillion, the biggest in the world.

Whilst these efforts are vital to support global economies during the pandemic, one must question if we are creating problems for years to come, as governments and central banks expand their indebtedness at an exponential rate. Nowhere is this more evident that in the US, where the Federal Reserve pulled out all the stops as the epidemic hit US shores, cutting its target interest rate to zero for the first time ever and injecting over $1.5 trillion into the economy (with more stimulus to come). Notably they also reduced the overnight reserve requirement to zero; historically US banks had been required to hold 10% of their liabilities in cash reserves. Two years of prudent fiscal and monetary policies to reduce the government debt have essentially been undone in mere weeks.



Source Visualcapitalist.com

So aggressive has the response been, that US government debt is forecast to exceed GDP (the debt-to-GDP ratio) for the first time since World War II, when it hit a record 106%.The IMF predicts this will also be the case in France, Spain and the UK and that in total, for advanced economies, average debt-to-GBP ratios will rise above 120% in 2021. This debt overhang may result in painful austerity for years to come. For countries that do not issue their own currency or those that struggle to refinance much of their debt, the situation will be notably worse.

Market breadth and what it means

It is our role to question the sustainability of the market rally since the March 27th lows and it is important to understand how these gains were actually generated. The S&P 500, for example, is being buoyed by fewer and fewer companies, a pattern that has historically led to extended drops in equity markets when eventually they break. But why has this falling 'market breadth' typically resulted in lower equity markets?

Looking at the S&P today, the index is down 17% from its all-time high (February this year), but the average media fall for all the constituents is a greater 28%. This is because approximately 20% of the index value is made up of just five stocks: Facebook, Amazon, Apple, Microsoft and Google (Alphabet), commonly referred to as the 'FAAMG'. It is notable that NASDAQ Composite index, where these same five stocks account for nearly 50% of its value, is down less than 3% for the year. As investors plough money into this small group of popular stocks, it masks the true performance of many other companies. Without an improvement in the laggards (the majority at this juncture), the market remains vulnerable to the fortunes of these few companies. Whilst we can expect technology-focused companies to prosper during and post-COVID-19's landscape, nothing is for certain and cracks may appear. Only this month, Amazon shares fell almost 10% in a single day as it incurred unexpected costs for protecting its infrastructure from the virus. Many are now questioning: in a world where over twenty-five million are unemployed in the US alone, how much additional demand for cloud computing, expensive smartphones and the like will there actually be in the coming years?

With the initial wave of pandemic panic subsiding, attention now turns to company earnings. Whilst Q1 earnings show a modest downturn, the real lockdown impact will not be seen until the end of Q2 in July and August. We expect then a further wave of weakness in certain companies and industries.

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Given our current equity allocation and higher-than-usual cash position within portfolios, we see this as a perfect opportunity for active fund managers who can seize opportunities and accumulate positions in strong companies trading at undervalued levels.

Long-term economics: The pain before the gain

It is clear that most global economies are in or facing recession this year. The classical definition of a recession is six months of negative GDP growth. On this basis, France and Italy are already in recession and, based on the first quarter fall, the US and UK are as well, although we will not have official confirmation until the August release of Q2 figures. The IMF predicts a 6.0% drop in GDP for the US this year, 6.5% for the UK and a huge 9.0% for Italy. Overall, the global economy is expected to shrink by 3.0% over the year, marking a steeper decline than the 2008 financial crisis and the worst since the Great Depression. Even these dire forecasts could prove to be overly optimistic. So how bad will it become and how long will it last?

At the start of the epidemic it was suggested there would be a sharp rebound in economic activity in the third quarter of this year as lockdowns were lifted and everyone got back to work, with life returning to near normal. However, this 'V'-shaped recovery is looking less likely as time marches on, with no confirmed cure and lock-down prolongation to avert a 'second-wave' of infection. As long as human interaction remains dangerous, business cannot reasonably return to normal. It seems reasonable to expect restrictions to last well into the third quarter, albeit at ever-reducing levels, which will surely push any recovery into the fourth quarter at best, or more likely into the New Year. And let us not forget what the new 'normal' will look like: people will certainly be less inclined to be in crowded spaces, whether in the office, transportation system or shopping malls. Restaurants and air-travel for example, will never be the same again.

It is clear that despite governments' best efforts to save jobs through furlough schemes and business support, millions will never be able to return to their current jobs and unemployment is sure to rise. In the US where employment figures are published more frequently, 30 million have already filed for benefit, leading to estimates that the unemployment rate has in reality already risen to 16%, the worst since 1939. In the UK, with over a quarter of all employees furloughed, it is also becoming clear that some will not have jobs to return to. A higher unemployment rate will result in a fall in household income, and combined with a fall in consumer sentiment, it will lead to lower household and consumer spending, which accounts for the highest contribution to GDP. Such a scenario will certainly make any economic recovery to pre-COVID-19 levels slow and painful for many. Corporate earnings will likewise fall and today's heady valuations for equity markets will become unsustainable. In such a fluid situation where we swing between fears over a rising infection rate to euphoria over potential vaccines, it is impossible to predict with any accuracy what the final outcome will be. However, what we can positively say is that short-term damage has been inflicted on the global economy, that we must be prepared for significant medium-term damage and, depending in the length of current epidemic, long-term damage may be felt for years to come.

Such a scenario steers us away from more cyclical sectors of the economy and towards companies with strong balance sheets, strong moats and business models that are compatible with the 'new normal'. We are focusing on more defensively orientated managers that should help dampen future market volatility from our portfolios.

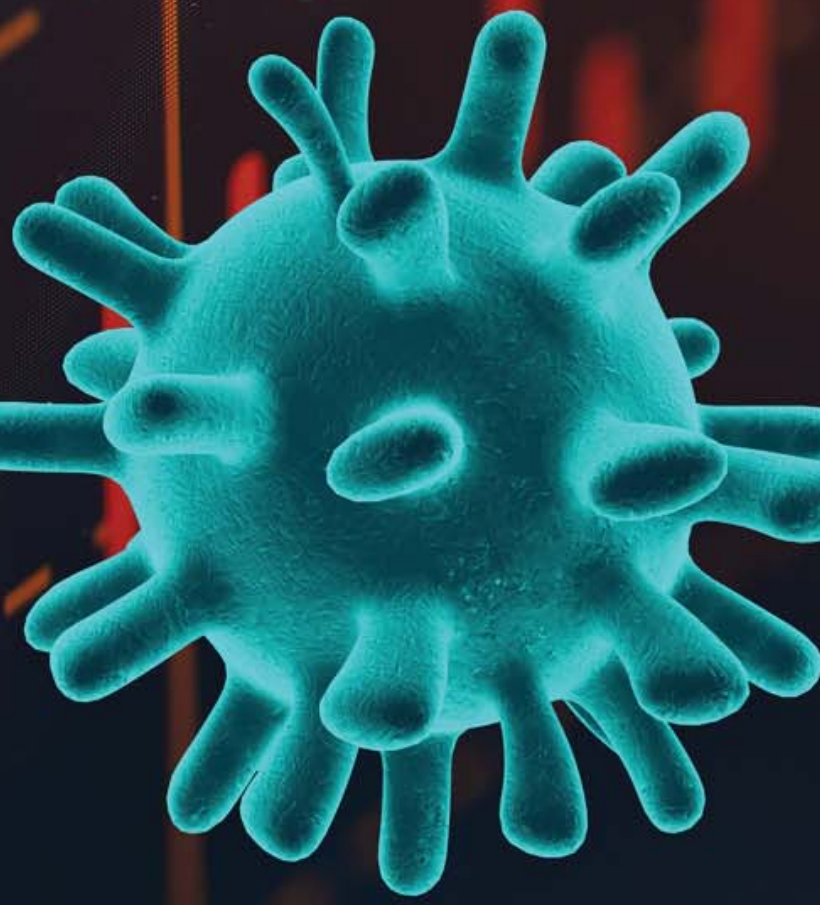
Winners and losers: How so the NASDAQ?

Whilst nearly every sector of activity has been negatively affected, some such as healthcare, are clear winners. Of these winning sectors, technology has been the largest beneficiary during the current crisis as more and more households turn to online shopping, businesses turn to cloud computing and social media and video conferencing become the norm. The NASDAQ 100 Index, with an 89% weighting to technology, communication services and consumer discretionary sectors, proves testament to this. Despite being still below its February high, the index is now almost flat for the year, outperforming most other sectors and the broader equity markets since March lows.

As we mentioned in our analysis of market breadth, the NASDAQ's strong performance can also be attributed to its make-up, dominated by five of the largest tech companies, the FAAMG, which combined represent 50% of the index. These five stocks have rallied strongly this year, driven not only by continued high growth (now aided by COVID-19 technological shift) but also due to their positions of undisputed market leadership and strong balance sheets with piles of cash. As investors focus on the long-term prospects for these companies rather than the short-term challenges, it is easy to forget they will also face headwinds during this period. Facebook, for example, will undoubtedly benefit from more users, but may suffer as corporate advertising revenues fall; it has been estimated that their ad prices could drop between 35% and 50% during confinement. Google faces similar challenges. Amazon has already reported the high cost of protecting its employees and facilities from infection, whilst Apple is still dependent on selling tech gadgets, hampered by store closures in China and the rest of the world. Similarly, Microsoft will suffer from reduced device sales however, its shift towards cloud services may insulate it somewhat.

Nevertheless, as we write, these companies continue to perform strongly, and the NASDAQ seems to have proven itself a justified investment in both bull and bear markets. Given the maturity and market dominance of the FAAMG, it is difficult to see where threats to their dominance lie.

Portfolios need a healthy exposure to this technology orientation within asset allocations.



Where it all began: China

With growing rhetoric from the US and other parts of the world regarding the origins of the coronavirus and China's complicity and failure to provide timely information on the original outbreak (if President Trump is to believed), we cannot rule out future trade restrictions, tariffs on Chinese goods and even demands for compensation. Such a Tiananmen-like backlash will certainly be detrimental to the Chinese economy, but as yet, this is merely speculation so we will focus on the economic reality as we see it now and ask whether it offers any road map for recovery in other parts of the globe.

Even before the virus outbreak in December, Chinese growth was weakening to its slowest pace in almost 30 years. Four months after the initial break-out, published figures show that GDP fell by 6.8%, the first reported contraction since 1976. China's three pillars of growth: consumer spending (down 19.0%), exports (down 13.0%) and fixed asset management (down 16.0%), all suffered as parts of the country were placed into lockdown in January and February to contain the virus. Importantly, figures for March looked marginally better as parts of the economy resumed work. However, unemployment remains elevated, and the much-anticipated boost in exports when China's factories and supply chains reopened, did not occur as it coincided with the start of lockdowns in other key markets.

The Chinese government's response has been decisive, pledging ¥4 trillion (or $565 billion) in aggressive infrastructure spending, including the construction of more airports, railways and power grids. This strategy worked well post the financial crisis of 2008, where growth rebounded to above 8.0% in two years. The IMF now predict that of all the major economies, only China and India will generate positive growth this year, although for China it will be at an anemic rate of 1.2%. If figures are to be believed, China reported a total of 82,880 coronavirus infections and 4,633 deaths. Today the situation has improved with reported cases at the lowest level since mid-January and most confinement measures lifted (although an inward travel ban persists).Citizens are free to work but must use a government approved health app to prove they are virus free, as well as regularly have their temperature taken and wear a face mask.

Using China as a case study, one can take comfort that draconian lockdown measures will prevent the spread of the virus and loss of life. Unfortunately, it also confirms that immense damage will be inflicted on the global economy and the rebound may not be as swift as originally anticipated.

'All men are created equal' Thomas Jefferson

The impact of the virus will not be the same for all global economies. When the pandemic fog is able to lift, some economies will suffer far more than others... there will be winners and losers. The deep economic downturn that we are bracing for and know is coming will have a disproportionate effect on those economies with

a) the inability to effectively work from home;

b) a heightened exposure to the transport, retail and hospitality sector; and

c) lower access to fiscal stimulus.

Economic crises without doubt expose and exacerbate any form of structural weakness. Global economies in the richer countries do converge in expansionary times and all do well. With regret, in poor times, the weak get weaker. This manifested itself in 2008, with the gap between stronger developed economies and the weaker economies expanding to 10 points. Who will lose out? Southern Europe again is at the bottom of the pile... Greece, Spain and Italy lose out on all three counts. Economics doesn't understand that man was created equal.

Global economies in the richer countries do converge in expansionary times and all do well.

Bad debts and banks: Not again!

The 2008 financial crash was predicated on poor lending, excesses in the financial markets and a lack of controls in core financial institutions. It led to the collapse of financial institutions and bankers were universally pilloried for their greed, leading to regulatory, legal and statutory changes in the years that followed.

It took the banks 10 years to overcome the stigma... and many didn't. City greed was a byword. This time rather than being at the vanguard of losses, the stability the banks have created is cause for some muted celebration. They are better prepared and controlled/regulated to face this economic maelstrom. They will, however, not find it easy as they will incur severe and substantive losses as a result of the pandemic impact on their corporate and personal loan books. The banks are in the frontline of economic loss, battening down the hatches, and preparing for the worst.

Cash strapped business are drawing down on credit lines, out of work employees are delaying loan and mortgage repayments, and governments are boosting outbound bank debt as deliverers of the country's capital. Some of these loans will never get repaid.

Outstanding loans at the top 4 banks in the US alone increased by $4trillion in the 12 months to date and this resulted in positive trading revenues. However, the new low interest rates will eat into the banks' margins.

Banks are now bracing for an avalanche of bad loans and in the first quarter of 2020 alone booked $24bn of provisions against possible credit loan losses. They have only scratched the surface of potential loan losses and it could take a further $100bn+ in loan debt write offs to stem the tide... but no one knows. There are no economic models in existence that that reflect GDP down by an unprecedented 30% and exponential growth in unemployment. Their guesstimates are just that.

It's uncharted waters, but the strength and structure of the big global banks means they are far better able to cope than ever before. The battleground may move from the health issue to the wealth issue all too soon.

"You only find out who is naked when the tide goes out"
Warren Buffet

Boom periods lead to greed and fraud. Heady growth periods help fraudsters paper over the cracks and hide dishonesty, often with the help of culpable and/or ignorant accountants. The biggest did get called to account. In the late 1990s Enron was found out by the dot com crash, exaggerating wilfully and fraudulently both its financial position and its profitability. Bernie Madoff's misappropriation of $65bn of client money in 2008 was debagged after the fall of Lehman Brothers. Japan's financial history is littered with "Ziatech" mismanagement (financial engineering) and the near collapse of some revered household names… Yakult Honsha springs to mind.

Market meltdowns cause a dash for cash and that's when the horrors of inappropriate management are stripped bare for all to see - it's a bad time for the crooks in finance. Even close to home there will be some indiscretions and fraud is on the up.

Nothing has hit the headlines to date in 2020, but it will happen. Small snippets are appearing, mostly petty profiteering and accounting smart moves, but surely we will see the "big one" before too long.
Please don't get me wrong, a very small percentage of companies are at fault but they can be disastrous for those involved. Moving earnings and revenue metrics around is relatively easy to accomplish for fast moving companies and trying to avoid bad news and the hard times by stretched interpretations of GAAP accounting standards can be "de rigueur".

If survival is threatened, lines get crossed and this can lead, when the tide retreats, to someone losing their trunks.

I would like to leave you with two quotes:

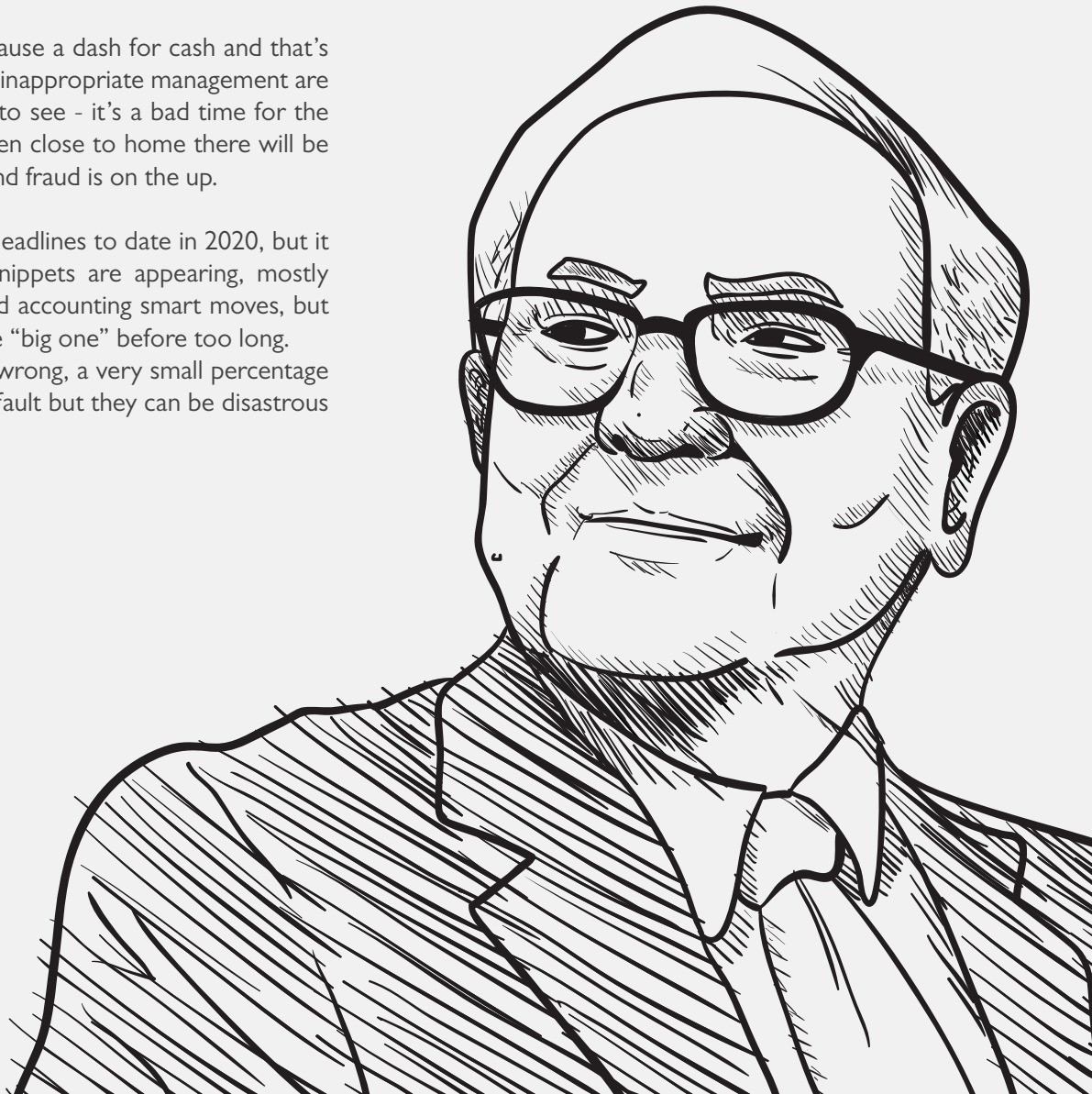
"COVID-19 is a perfect storm for fraud"

Bruce Dorris, Certified Fraud Examiners

"Amid such massive dislocation, someone will inevitably cheat"

Jules Krull, K2 Intelligence

So watch this space!



The elephant in the room: US vs. China

While markets are digesting the "honesty" of the derivation of the global COVID-19 pandemic from Wuhan, the elephant in the room is the relationship between the two largest superpowers, the US and China.

It has been an extremely eventful quarter for the global economy but there was one risk we thought we had put behind us in January, when Washington and Beijing agreed on a trade truce, termed the 'Phase One' agreement. In theory this put to bed the ongoing trade tensions between the US and China. Or so we thought.

However, unsurprisingly, relations have deteriorated in light of coronavirus, with both parties stepping into the battleground once again. President Trump is now playing the blame game, accusing China of intentionally creating, or at best allowing the release of the virus from a Wuhan laboratory, and criticising their efforts to contain the spread of the virus across the globe. His heightened rhetoric came just as the Chinese economy begins to restart after several months of lockdown. Perhaps it was just the excuse Trump needed to restart the ongoing trade battle. Such a battle could lead to further damage to the US economy.

Tsun Tsu, the greatest Chinese militarist, expounded the philosophy of not extending your supply lines in battle. Does Trump know something we don't? Or is he choosing the wrong time to pick a fight?

Rather than the two largest economies in the world coming together in a co-ordinated effort to battle the virus, it seems they are focused on their own independent agendas and more concerned with victory in their trade war.

As it stands today, it looks as if President Trump could disrupt the trade deal if Beijing fails to follow through on its planned purchases of US goods. His further threats extend to raising tariffs on Chinese imports. An unravelling of the trade truce is now becoming a real threat, which could very well endanger any post-COVID-19 global economic recovery.

Unfortunately, if we see an escalation of trade tensions once again, this will act as a severe drag on the post-pandemic recovery in global markets and may further dampen potential investment returns for months ahead. The elephant is being monitored closely.

The move to ESG: The planet has a rest

It's fair to say the global lockdown has given our planet a brief respite from the pollution caused by human activity, making it perhaps one of the only beneficiaries of the events of the last several months which have caused large scale disruption to the lives of the global population.

Once this is all over, we will reminisce about those days when our air was cleaner, our skies were free from the condensation trails left by aircraft and the only sound outside our windows was the birds singing. It was a time when we could fully experience the beauty of the world around us, as stars shone brighter than ever, dramatic mountain ranges in Asia became visible once again, and for the first time in 60 years, the depths of the Venice canals could be seen as motorised boats and giant cruise ships had disappeared.

But why should we reminisce about these times when we could all contribute to making this a more permanent reality? The recent events of COVID-19 have undoubtedly shone a spotlight on the topic of ESG investing which was already well underway to transforming the investment landscape. The pandemic has highlighted just how fragile our planet, as well as our economy is, and how these can come under great threat if sustainability is not considered. Many companies performing well on ESG issues were already outperforming before the virus hit and managed to continue that outperformance during the turbulence within global markets, highlighting the capital protection capabilities which go alongside the environmental and social benefits.

TAM's range of risk-graded ESG investment portfolios now celebrate a proven 6 year track record, with some portfolios outperforming their benchmarks by over 40% since inception.

While the lockdown has given our planet some time to heal, it is a wound that could easily be reopened if we don't use this experience to make changes to our behaviour, including our investment decisions. Not only have we seen first-hand the tangible benefits we could experience from a cleaner planet, we have also seen how our investments could be protected at the same time, through owning companies that are not only addressing these environmental issues, but which also have robust corporate governance and high quality business practices. It is these companies which have proven their ability to fare better in testing times and which we believe are ultimately best-positioned for the future.

The future is bright, the future is green!

Brexit: What on earth has happened to that?

A once favourite topic for speculation by markets and investors has become yesterday's news in the face of COVID-19 but that doesn't mean it's subsided or gone away. Negotiations need to be commenced and concluded, legislation needs to be agreed and trade arrangements need to be cast.

What COVID-19 has done is wipe out a large chunk of the negotiating time needed to strike a deal. What we will see in the media and markets is a slow transition from COVID-19 headlines back to Brexit related headlines as we move closer to the December deadline.

With respect to the deadline in December it's a widely held assumption in markets, by voters, the mandarins of Brussels and Whitehall that it's going to be virtually impossible to agree any sort of a trade deal in time for this deadline. With mounting pressure on Boris to back his commitment to leave without a deal in December the UK government seems to be digging its heels in. COVID-19 has taken centre stage but the deadline for Brexit remains fixed. We continue throwing accusations at the EU about their reluctance to agree to a Canada style free trade agreement.

Brussels' rebuttal to this centres around the UK's proximity to the EU and the unfair advantage this would give them in terms of trade. The issue of proximity is not one which affects Canada which is essentially why their deal was easier to agree. In reality it took Canada 22 years to design their trade deal and another 7 years to get the EU to sign to it. Boris needs to recreate a British version in seven months.

This impasse on moving the negotiation deadline and the enormity of the deal being discussed is why investors should expect Brexit related volatility around UK domestic stocks and the currency later in the year. A meaningful pick up in media attention and the headlines is likely as soon as COVID-19 begins to fade from the market's psychology. Brexit is not dead, it's in a short term coma.

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Custody: The need for strength and stability in a crisis

One of the things that we all expect is security and stability of our financial institutions in a crisis. Custody, settlement and administration agents and remote working can work very well or they can fail miserably. Tales of some companies and service providers not meeting the highest standards and slow response times are being compared to the "business as usual crowd".

In good times it's never a one size fits all approach and COVID-19 is highlighting the wheat from the chaff. Who is delivering, who is on hand, who is picking up the phone and where are response times good or bad? It's all about solidity and strength in depth.

The security of clients' investments is paramount, which is why we do not seek to hold client assets directly and instead investments are typically held on our behalf with our custodian - Pershing Securities Limited, who:

- Have over 600,000 clients with assets of over $1.9 trillion.
- Are part of The Bank of New York Mellon Corporation (BNY Mellon), one of the largest and strongest financial institutions in the world.
- Are unparalleled in terms of their size, security and experience in custody and clearing services.

TAM have been protecting clients' assets with Pershing for over a decade. By partnering with the most respected counterparties, we provide clients with some of the highest levels of protection available in the industry.

The digital future in investment advice and management

The future seems quite uncertain as far as staying in touch with the intermediary community is concerned – even if lockdown measures are relaxed, a return to business as usual in the sense of 'popping into people's offices for a chat' may still be a long way off as social distancing looks to stay with us for the foreseeable future. Even if the government were to say it's safe to carry on as we did before the COVID-19 outbreak, it would be understandable for people to be a bit wary for some time to come.

Implementation of third party technology systems such as GoToMeeting, Zoom and the like enables us to screen-share documents and presentations, whilst engaging with each other via video (the closest you can get to a face-to-face meeting, and a small taste of 'normality'). A strong contention is that meetings have become more efficient as a result, and the sheer number of people you can speak to in a day has grown significantly. Producing a webcast channel through BrightTALK allows investment management teams to produce relevant content on a regular basis. We should all be making sure presentations are as relevant as possible, including audience feedback as to content.

These processes will stay in place beyond the current climate as it makes for smarter and more efficient business dealings with the target audience – we want to be able to support clients as much as possible and will endeavour to keep looking for ways to improve. In short, between the avenues mentioned above and simply picking up the phone, it's never been easier to talk.

COVID glossary

Bounce Back Loan – A government inspired loan scheme that enables business to access finance more quickly during the COVID-19 outbreak.

CCCF – Stands for COVID corporate financing facility, a package of diverse measures arranged by the government for temporary, targeted and timely support to business.

Community Spread – Refers to people that have been infected with the coronavirus in a certain area, including some who don't know how or where they became infected.

Containment Strategies – Are used at the beginning of an outbreak. It helps officials track the spread of the virus or disease within a community and then uses isolation or quarantines to keep those infected individuals from spreading the disease to other people.

Coronafobia – The fear of returning to work in case you should be exposed to COVID-19 germs and catch the illness.

Covexit – The process of gradually relaxing and removing the restrictions on public life imposed by governments in response to the Coronavirus crisis.

Covidiot – Someone who ignores the warnings regarding public health or safety.

Dash for cash – The term used for investors that rush to sell any asset they can in favour of cash.

Fallen Angel – A bond that was initially given an investment-grade rating but has since been reduced to junk bond status. The downgrade is caused by a deterioration in the financial condition of the issuer. The term is also sometimes used to describe a stock that has fallen precipitously from its all-time highs.

Flattening the Curve – The effort to reduce the spread of the COVID-19 infection in order to limit the number of cases at a given time to protect the health system from being overburdened.

Furlough – A temporary leave of employees due to special needs of a company or employer, which may be due to economic conditions of a specific employer or in society as a whole. These involuntary furloughs may be short or long term, and many of those affected may seek other temporary employment during that time.

Future Fund – A government backed £500mn loan scheme allowing access for Innovative and high growth UK business by way of convertible loan principally in technology, life sciences and creative industries.

Herd Immunity – A form of indirect protection from infectious disease that occurs when a large percentage of a population has become immune to an infection, whether through vaccination or previous infections, thereby providing a measure of protection for individuals who are not immune.

Immunocompromised – People who are immunocompromised have a weakened immune system, meaning their white-blood-cell counts are low or they have other conditions that make it harder to fight off infections and diseases.

Incidence – Refers to the number of individuals who develop a specific disease or illness (like COVID-19) during a given period of time, according to the CDC. The incidence rate is the number of new cases of a disease existing in a population at a specific time divided by the total number of people at risk for that disease in that population.

Pandemic – The global outbreak of a disease; pandemics are usually classified as epidemics first, which is when a disease is spreading rapidly in a particular area or region.

Physical distancing or social distancing – The deliberate increase of physical space between people to keep them from spreading illness. Experts recommend staying at least six feet away from other people to reduce your risk of catching the coronavirus.

PPE – Stands for personal protective equipment, worn by healthcare workers to reduce exposure to the coronavirus.

Quaranteams – The group of people you choose to live with during the coronavirus pandemic.

R Number – Refers to a disease's transmission rate or ability to spread between people. Sorry, this video isn't available any more. The higher the number, the more people who can get infected with a virus by just one person.

Unlockdown – The step-by-step process by which the government is attempting to have workers return to their normal operating environments.

Viral Load – The amount and quantum of viral infection that an individual is exposed to.
Viral Shedding – he term for a virus replicating inside the body and releasing into the environment.

WFH – Stands for working from home. The abbreviation is often used in digital communication to notify colleagues that someone is working from home on a given day or for a temporary period instead of regularly reporting to a physical place of business.

Zoombombing – The unwanted intrusion into a video conference call by an individual, causing disruption.

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A NEW NORMAL

Navigating through an evolving financial landscape during a pandemic

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