SPECTRUM
Asset Management

COVID-19: A Macro Outlook

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Brexit, trade wars, domestic and external country conflicts, Hong Kong oppression, Russian international cyber hacking, and populism still exist. However, these and other macro concerns have been eclipsed by the COVID-19 pandemic which has led to the first recession since the Great Financial Crisis (GFC). Some developed economies have lost a decade or more of growth. **Though we do not expect a V-shaped recovery, the US and Europe could experience GDP growth beginning in the second half of 2020. Banks and insurers should post lower profits this year, with no solvency worries.**

COVID-19 has significantly impacted world economies and our way of life. The virus has caused hundreds of thousands of deaths, and infected millions more, some recovering with debilitating or life-threatening maladies. Health protocols like working from home, lockdowns, social distancing, protective masks and quarantines are helping to slow the infection rate and alleviate hospital capacity problems. These safety measures, however, also have had unintended consequences. Low or no demand in 2020 for many products and services have crippled oil, auto, restaurant, air travel, lodging, tourism, real estate and other industries. Millions are unemployed as many small to medium-sized businesses have suffered lost revenues or bankruptcy.

Despite the uncertainty of a second infection wave, or the later-than-expected timing of a successful vaccine, we emphasize that *this is not a "2008 moment" for financials.* In the GFC many big banks collapsed or were rescued with taxpayer funds due to faulty loans, high leverage and inadequate liquidity – all recipes for systemic disaster. Today, bank balance sheets are solid with good asset quality and robust capital levels. *Unlike in the GFC, US and European banks are fundamentally well-positioned to help support an economic recovery by continuing to make loans to consumers and businesses.*

The US economy contracted by 9.5% in 2Q20, year over year. The country is enduring destructive politicism and social unrest. Tensions with China are heightened. The upcoming elections will be a referendum on quality leadership. But regardless of who is elected, the US should continue as the largest and strongest global economy, sustained by ongoing enormous fiscal capital infusions and Fed support.

COVID-19 pushed the European economy from weak to worse. GDP contracted ~15% in 2Q20, year over year, including double digit percentage declines in Spain, Italy and France. The UK is estimated to have a GDP decline of around 20% in 2Q20. Brexit is a long-standing challenge as Prime Minister Boris Johnson is determined to leave the EU by the end of 2020, even without mutually beneficial trade and other important agreements. PM Johnson and the Bank of England should, however, move the UK economy into recovery over time. Likewise, the ECB, fiscal union and national governments are prepared to support the European economy with whatever means necessary. *Though the EU and its banks generally lag the success of the US, it should be recognized that Europe is the second largest economy in the world.*

We note that our long-standing defensive style of fundamentals-based credit selection includes the review of important environmental, social and governance (ESG) issues. Needless to say, pandemics and other health concerns will be perennial ESG concerns for sovereigns, industries and companies. **Spectrum has a stable but cautious credit outlook due to prevailing macroeconomic, sovereign and political risks. COVID-19 is a not a credit event for the names in which we invest.**

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