

A Quarter in the Markets

Q1 2021

We are pleased to introduce our latest edition of 'A Quarter in the Markets', which provides an insight into financial markets from the Multi-Asset Solutions team at Santander Asset Management UK.

Key factors influencing markets

There was a sense of optimism in the air in the first three months of 2021 as the vaccine rollout gathered pace and investors began anticipating economies would re-open later in the year. This had two immediate effects on stock markets. First, the prospect of increased economic activity caused shares to rise in companies that have been hit hard by the pandemic, such as the services and travel sectors, as well as oil and commodities. Second, bond prices fell as investors anticipated that higher growth would cause inflation to rise.

Overall, global stock markets performed well over the quarter, with shares once again outperforming bonds. However, there were clear performance differences between regions and sectors, with the UK, US, Japan and Europe in positive territory, and China and Asia Pacific falling over the quarter.

So, what happened during the quarter?

It was a fairly good quarter for investors, although this was not without a few bumps along the way. The key driver of markets during this period was once again the COVID-19 pandemic, with the vaccine rollout around the world taking centre stage. The success of the vaccination programmes in the UK and US, where significant portions of the adult population have been vaccinated and hospitalisation rates have been falling, caused investors to look ahead to the potential for a sustainable re-opening of economies. As a result, shares in companies that had been negatively affected by the pandemic rallied.

By contrast, technology companies and government bonds struggled over the quarter. Benchmark bond prices fell as investors favoured shares in anticipation of higher inflation and rising interest rates.

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Technology shares, which soared throughout 2020, fell sharply in February. This was driven by the expectation of a re-opening economy as well as concerns about rising interest rates. Given that some technology companies often borrow large sums of money to fuel their growth, higher interest rates may negatively impact their returns.

How did different economies react?

The start of the year was challenging for the UK as the country entered another lockdown intended to slow down the spread of COVID-19, while supply chains were disrupted by the onset of the new trade agreement with the European Union (EU). The economy struggled during this time, as business activity in the services sector - which includes hotels, restaurants and other customer-facing businesses - entered a downturn. The manufacturing sector was in better shape, although supply chain disruptions caused by lockdowns and post-Brexit shipping delays dampened growth slightly early on in the quarter.

By the end of the quarter, the UK's economic situation had improved slightly as both the services and manufacturing sectors saw increased activity in March, the highest rate of expansion for seven months. Much of this was attributed to the successful vaccine rollout, which saw more than 30 million people receive their first dose by the end of March.

Europe's economy also suffered over the quarter, but the main story was the limited rollout of COVID-19 vaccine programmes and the slow implementation of the EU's financial relief programme for the pandemic. Much like the UK, Europe's economy struggled as a result of stringent lockdowns aimed at slowing the spread of COVID-19. While the manufacturing sector remained in good shape, activity in the services sector contracted. A major driver of this growth in the manufacturing sector came from Germany's construction and manufacturing companies, which recorded strong demand throughout the quarter.

In January, the US saw a change of government as Joe Biden was sworn in as president and the Democrats gained control of both the House of Representatives and Senate. This marked a major change of direction for the country, which was previously snarled in political gridlock under President Donald Trump and a Republican-controlled Senate. During a time when COVID-19 infection rates and unemployment stood at high levels, President Biden unveiled a \$1.9tn recovery plan aimed at providing relief for people and businesses affected by the pandemic. He also pledged to speed up the distribution of vaccines.

The US faced many of the same challenges as other developed countries with the pandemic continuing through the winter months, although by the end of the quarter the economic situation had improved. With a vaccine rollout that has been among the most successful in the world, there was a noticeable increase in economic activity over the quarter. Restaurants have begun to re-open, retail sales have improved and air

travel started to rebound. Nevertheless, unemployment remained at high levels, with nearly 19 million people out of work. In Asia Pacific, there was clear evidence that China's economic recovery was well ahead of many other parts of the world. Manufacturing output in the world's second-largest economy continued to grow over the quarter and accelerated in March following a brief break over the Lunar New Year in February. Taiwan is also on a strong footing and has forecast that its economy will grow by 4.6% in 2021, its fastest pace since 2014. Taiwan is a major exporter of computer chips and is benefiting from high global demand for technology products. In Japan, there was strong demand from China for its technology exports, but the domestic economy has struggled after the government implemented new COVID-19 restrictions. However, there were concerns that the economic recovery was stalling in Japan, with government data released during the month showing that industrial output fell in December.

What is the outlook for markets?

Looking to the months ahead, we remain cautiously optimistic in our outlook. As we have written previously, the route for markets and economies in the coming months is linked to the path of the COVID-19 pandemic. The worldwide vaccination effort, combined with warmer temperatures in the spring, may allow economies to begin returning to some sense of normality later in the year.

Meanwhile, central banks and governments will likely continue to support economies and we believe this will be positive for stock markets. While shares have seen strong growth recently, in our view, there is more room to grow in this environment.

Find out more

Listen [here](#) to the latest **Market Views** from our Head of Multi-Asset Solutions, Stefano Amato, as he shares his thoughts on the main themes dominating markets.



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