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Dear Client,

This is a brief bulletin to keep you up to date with our views and strategy following the global stock market correction last week.

In order to increase portfolio resilience in the face of the risks stated in our January management report we started the year by taking some profits in riskier, “high beta” areas of the portfolio that had performed well in 2019 (such as High Yield bond funds, more aggressive equity funds). We reinvested into high quality, lower volatility assets.

Then emerged the globalization of the Coronavirus as a real “Black Swan” event out of left field. Markets have been quick to price in a very negative economic scenario.

At this point, measures taken to contain the flu (cancellation of meetings and events, closing of factories, travel restrictions) are the main cause of falling growth forecasts. China has clearly taken the most dramatic measures of containment, with some success: new cases in China are declining rapidly. The near stand-still in the Chinese economy and production will reverberate as a "supply shock" to its many trading partners in the global supply chain, and will have a negative effect in the first half of the year, with a subsequent sharp bounce back.

What is still unclear is the extent of lasting damage to Chinese consumption (which would be a demand shock), if small private enterprises cannot afford to keep paying wages. The Chinese government has put measures in place to provide credit lines to companies, but it is hard to foresee how well these will work. In spite of the Chinese economy having suffered the most draconian containment measures, its stock market is actually the world's best performing year to date, down by less than 1%.

With the virus having spread to many other countries, the extent of possible infections plus the containment measures that will be taken in these countries are still unknown. The latter are likely to be less severe than in China. If infections follow a similar trajectory as in China, the number of cases worldwide should peak about 2 months from now. It is impossible to estimate at this point what the total effect on global growth will be. Also, the extent to which the "fear factor" will depress consumer spending, which had been a bright spot in both the US and Europe until very recently, is hard to predict.

In the case of a benign scenario, renowned economists estimate that global growth will be 2.2% this year (after 2.7% in 2019). At the other end of the spectrum, they see that in a less benign scenario global growth could fall by 0.5%. This is a very wide range of possibilities.

On the flip side, Central Banks will not stand idly by, and it is widely expected the Fed will deliver 2 rate cuts in coming months. Also, fiscal support can be expected in badly effected countries. On the date of writing (2nd March) markets are rebounding after supportive comments from the Fed and injections of liquidity from the Bank of Japan. Though rate cuts are no cure for the virus, monetary and fiscal measures can at least soften the blow and support sentiment.

In our experience of past corrections and crises, trading “after the horse has bolted” and when markets are volatile is counter-productive and costly. We will therefore stick to our current well-diversified strategy, having recently bolstered the quality of the portfolios. We are still underweight equities; when the time is right we will be looking to increase equity weightings back to neutral as value re-emerges in the stock markets.

Please do not hesitate to contact us should you have any questions.