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WEALTH
REVOLUTIONARY THINKING

MARKET NOTES

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Flying the global economy into the ground from 35,000 feet will go down as one of the most difficult and controversial decisions in the history of mankind.

The coronavirus is an elusive adversary and limiting the tragic loss of life so far to 325,000 has been a hollow victory, achieved at a very heavy price in the form of record job losses and the destruction of several hundred million livelihoods. The sooner the world is open for life and commerce again, the sooner the long recovery phase can begin.

The economic wreckage will take years to clear up. However, there are several reasons to be optimistic for the future. The quarantine measures appear to have been effective in slowing the spread of the virus and the pharmaceutical industry is rumoured to be closing in on a cure. As with other pandemics, history suggests COVID-19 will pass with time and the global economy will begin the healing process from this self-inflicted wound. Several countries in Asia have already flattened the curve and economic activity is slowly returning to normal. The same can be said for Europe and in parts of the United States. This cycle of recovery is spreading across the globe, supported by record low levels of interest rates, debt moratoriums and trillions of US dollars of fiscal stimulus packages.

Liquidity is key in the current trading environment and we expect most markets to remain range bound until the economy re-opens.

Only then we will begin to fully understand the extent of the damage caused by the economic shutdown. For the time being, the playbook is essentially unchanged from the Global Financial Crisis, where positioning in liquid markets paid huge dividends during the recovery phase.

- Fixed income: we are overweight investment grade credit and TIPS, and underweight government, high yield, and emerging market bonds.
- Equities: we are overweight quality stocks in the US and Asia with a tilt towards the healthcare and technology sectors, underweight all of Europe and our emerging market exposure is skewed towards Asia, specifically oil importing and virus-light countries such as China, Taiwan and South Korea.
- Currency: we remain negative on the euro and positive on sterling, especially versus the US dollar.
- Commodities: we are overweight physical gold.

FINAL THOUGHTS

The equity markets are pricing in a sharp, V-shaped recovery and limited collateral damage from the lockdown. This is possible but increasingly not our base case. The funding required by the various governmental parachute programmes is going to cast a very long, dark shadow over debt markets for at least the next decade. Central banks, via their bond purchases under QE, are essentially printing money and this will lead to inflation and potentially hyper-inflation within the next 2-4 years. Also, the bankruptcy rate is expected to rise significantly once the lockdown is lifted and bond holders in the riskier credits will suffer material capital losses.

The roadmap in the short-term is to keep it simple and liquid, favouring equity of quality companies with positive cashflows and hard assets such as gold, avoiding the high yield and CMBS sectors at all cost.

In the words of the famous economist, John Maynard Keynes,
"markets can remain irrational longer that you can remain solvent".

It is a time to play defence and preserve capital until the damage from the lockdown has been determined – Q4 at the earliest.

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