cadiz
ASSET MANAGEMENT

CORONAVIRUS

A look-through approach to the Global Risk

PROVIDING PERSPECTIVE IN A TIME OF MARKET RISK AND CONCERN

As at 16 March 2020 globally there are currently 173,285 confirmed cases with 6,668 deaths from the COVID-19 outbreak. The number of recovered/discharged cases stands at 77,789, with only about 7% (5,937) of all active cases seen as serious or critical.

If we compare this to the SARS virus of 2003, there were 8 096 confirmed cases with a fatality rate of 9.6%, compared to the fatality rate of COVID-19 of 3.5%, (which is an inflated statistic due to the significant number of cases that are not reported and in which the patient recovers), this means that COVID-19 is more infectious, but significantly less fatal than SARS.

Moreover, the age and health profile of COVID-19 mortality rates is skewed due to the death rate being as high as 14% for people over the age of 80 years and patients with pre-existing medical conditions like cardiovascular disease or diabetes.

WHAT DOES THE COVID-19 OUTBREAK MEAN FOR THE WORLD ECONOMY?

Global economic activity will be impacted by a slowdown in manufacturing which is caused by the closure of factories and workers being absent, as authorities attempt to curb the spread of the virus. With the supply-side of global economy under pressure, the demand-side will also naturally decline due to less travel and tourism. We have already seen sporting events either cancelled or played in closed stadiums with the Bahrain F1 Grand Prix to take place behind closed doors, along with a slowdown in retail activity.

The virus outbreak has also created a fall in global risk appetite as investors move from riskier assets, like equities, into perceived safe havens such as US government bonds, as they attempt to understand the likely impact on company profits in the coming quarters. This has led to a sentiment-driven decline in the world stock markets due to an overreaction in selling. This, however, creates an opportunity for long-term investors to acquire quality companies at fundamentally attractive valuations.

Encouragingly, policy makers have shown a willingness to create further liquidity and provide monitory policy stimulus in the form of interest rate cuts from the US Federal Reserve as well as other central banks around the world. The G20 group of leading economic nations have indicated they are willing to use appropriate measures to support the global economy.

At the same time, oil prices have plummeted to around $35 a barrel. This selloff follows the news that Saudi Arabia is set to increase production next month as talks between OPEC and Russia to cut oil production, to support the oil price, breakdown. In the medium term, however, a fall in oil prices due to increased supply could be positive for the global economy as this acts as fiscal stimulus for consumers and lowers inflation expectations for central banks.

Nonetheless, in the short-term, the lower oil price has an impact on certain sectors of the economy and will add additional pressure to credit markets. Both of these we will watch closely.

WHAT SHOULD INVESTORS DO?

At present, there is significant concern around world markets regarding the effects the COVID-19 virus will have on global growth. In times like this, market sentiment often runs ahead of fundamentals, exposing investors to unnecessary downside risk.

It is our job to identify which opportunities look attractive, versus which opportunities are attractive. Getting these calls right and staying the course will benefit all of our clients.

Markets have endured a dramatic reassessment of valuations in recent weeks with the fall in both equity prices and bond yields, and while we anticipate that this may continue for some time, we believe that trying to time the market during these volatile times is near impossible.

Our advice to our clients during times like this is to stay calm, ride out the turbulence and markets will correct themselves.

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