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WEALTH MANAGEMENT

Coronavirus - Market update

April 3rd, 2020

Since I wrote ten days ago, markets have rallied off their bottoms and news flow around Covid-19 (and almost nothing else) has continued at a pace - anyone remember Brexit? The pace of deaths in Italy and Spain appears to be slowing, though each day that passes reminds us of how contagious this disease is. The US is about to enter a two to three-week period where both the medical and economic facts are likely to shock, and this leads me to suspect that we may not have seen the market bottom quite yet.

Recession is now a given and it is only a matter of what the quantum will be. Needless to say, it is likely to be significantly worse than in the global financial crisis 12 years ago.

You cannot shut down global commerce to the extent that is currently been undertaken, without very material economic impacts. Hospitality, leisure and of course airlines are being hit particularly hard. BA have announced they are furloughing 36,000 employees and have agreed a 50% pay cut with pilots for the next two months. In addition, EasyJet have understandably grounded their entire fleet of aircraft with no travel permitted across Europe. No one of course has any visibility right now as to when we can return to the skies.

Based on what we know, it looks like global GDP in 2020 will contract by around 3% and for context, that is twice as bad as in the global financial crisis. This will be only the second $ based global GDP reduction in the last 50 years.

We have just learned that last week 6.6 million Americans applied for jobless claims taking the total for the last fortnight to 10 million, a truly staggering number and an indication of the seriousness of the position in the US. For context, the previous largest weekly number to sign on for jobless claims in the US was in 1982 at 695,000.

Coupled with that, today we saw the release of US payroll numbers, which revealed that 700,000 lost their jobs in March (the expectation was for 100,000) and the first monthly reduction since 2010. The expectation is that the April numbers will be much worse, and this will almost certainly lead to double digit unemployment in the US in short order.

US citizens do not benefit from social benefit systems to the same extent as Europe and neither do they have the 'free' medical benefit systems that we have access to in Europe. These are therefore extremely worrying numbers and why the US government will shortly be paying a one-off lump sum of circa $3,500 to each American family of four - so called helicopter money. 175 million Americans will benefit, and this is the largest domestic benefit package ever orchestrated in US history.

Rosan Helmsley Ltd, 1000 Cathedral Square, Cathedral Hill, Guildford, Surrey, GU2 7YL | 01483 90 40 40 | www.rosan-ifa.com

These are of course heroic numbers in totality - over $2 trillion - and if the lockdown is anything but short term from here, the measures will provide small respite against the unemployment numbers we are witnessing. This matters as we all recognise that the health of the US economy is paramount to driving global growth and economic health.

Debt is a real problem on the other side of this crisis

There are other headwinds to be concerned about on the other side of this crisis - debt being my number one concern, and of course the world is unlikely to be debt free anytime soon. Whereas, I remain confident that we will eventually all emerge from this crisis and markets will come back, I am very concerned about the debt levels building globally - debt at personal, corporate and government levels are at all-time highs and we are now adding another huge layer through combined government response to this crisis.

Global debt grew to an all-time record in the first nine months of last year by $9 trillion to almost $253 trillion, according to the Institute of International Finance. That puts the global debt to GDP ratio at 322% surpassing its previous 2016 record level. More than half this number was accumulated in the developed markets such as the US and Europe where debt to GDP ratios are now approaching 390%. Ultimately, debt needs to be repaid and the impact of current policy on our children's futures is something we should all be genuinely concerned about.

Market Update

Whilst we are all witnessing significant reductions in invested portfolios through this period, it is important to understand that portfolio managers have been working very hard to restructure portfolios, both to mitigate additional risk and also to take advantage of opportunities that will naturally evolve through this process.

The scale and speed of the sell off was faster than anything seen to date in history and the concept of selling for medium to long term investors at these levels, and therefore crystallising losses, remains against my better judgement.

That stated, and as alluded to in my previous communique, this is a very different set of circumstances than any of us have witnessed in our lifetimes and given some of the comments made above, it is easy to see how markets could have another leg down before things get better. Many market commentators have suggested we have already seen the bottom and indeed that may turn out to be correct, but news flow is such that volatility (up and down) is sure to remain until we see visibility on the end of the virus itself.

As a way of gaining some view on what things might look like post this period, I have summarised data in the table below on stock market performance over one, three and five year periods following the previous 12 bear markets that are worse than this one.

This provides some rationale for remaining invested, though clearly, we are at a level of 30% down on main indexes from the peak in this downturn, and as can be seen from the table, some of the historic drawdowns have been worse than this.

Stock Market returns post the last 12 bear markets

			Forward returns		
Drawdown	**Peak**	**Trough**	**1 year**	**3 Years**	**5 Years**
-86.20%	07/09/1929	01/06/1932	162.90%	170.50%	344.80%
-56.80%	09/10/2007	09/03/2009	53.60%	97.90%	181.60%
-54.50%	06/03/1937	31/03/1938	35.20%	38.20%	84.50%
-49.10%	24/03/2000	09/10/2002	24.40%	59.00%	105.10%
-48.20%	11/01/1973	03/10/1974	38.10%	72.70%	117.50%
-40.60%	07/09/1932	27/02/1933	98.70%	194.50%	154.60%
-36.10%	29/11/1968	26/05/1970	34.70%	50.60%	42.20%
-34.50%	09/11/1940	28/04/1942	61.20%	128.60%	144.90%
-33.50%	25/08/1987	04/12/1987	23.20%	55.50%	121.70%
-31.90%	25/10/1939	10/06/1940	8.00%	59.70%	118.80%
-31.80%	06/02/1934	14/03/1935	83.80%	16.30%	84.90%
-29.80%	18/07/1933	21/10/1933	2.90%	120.10%	87.30%
-29.20%	19/02/2020	?	?	?	?
		Average returns	**52.23%**	**88.63%**	**132.33%**

What is interesting is that there are no loss years in the one, three and five year periods that follow significant bear market downturns. Obviously, this time could be different, but of note is that before the onset of this crisis, the world was not in bad shape - yes global GDP was slowing but most markets were trading well and therefore it is not unreasonable to assume that a market bounce back could be robust. Ultimately, that will depend on the length of the global shutdown and how governments trade off further health risks against getting the healthy back to work and productivity.

What next?

We are all adjusting to a very different way of living, working and communicating and it will be very interesting to see how our human experiences through this period dictates behaviour after it. My suspicion is that we will emerge with different perspectives on many aspects of life, on travel, on socialising, on work, but let's hope that we can all get back to 'normal,' whatever that is, as soon as we can.

We will continue to update our perspectives on the website on a regular basis through this period and do of course get in touch if you need to discuss any aspects of your financial planning. This was certainly the oddest financial year end we have had since incorporation in 2001, with the team working remotely but retaining full functionality and service to our client base for which I am very grateful to all our team.

Rob Sandwith | Chief Executive

rob@rosan-ifa.com

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