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February 2020 Market Wrap — Monday 2 March 2020

Broader global equities declined sharply in February, as fears of the spread of the coronavirus and it effect on the Global supply chain and potential economic impact weighed on markets. All global markets had their worst week since the financial crisis. The fear of the unknowns captivated investors' minds and market last week.

While the ghost of 2008 may loom larger the comparison is unfounded and extreme to say the least. Thursday was the largest traded notional dollar amount ever traded in the US equity market (786bn) and the largest day of buying for Long/Short funds since Feb 2018. The +10% pull back over the past 7 trading days is the fastest ever and only four other times have we seen a -10% down week since WWII (October 1987, April 2000, September 2001, and October 2008).

I wanted to revisit how this sell-off compares to similar events we have witnessed in the past, specifically 2003 SARS, 2014 Ebola, and 2015 MERS as the S&P is now down 15% from its recent all-time highs. During the 2003 SARS outbreak, the news flow peaked by the end of April 2003. The S&P 500, however, troughed about a month earlier on March 11th. From the initial outbreak to trough peak to trough the S&P was -4.2%. The 10 days post +9.2%, with 10Y yields toughing at 3.56.

The 2014 Ebola outbreak lasted longer than the respiratory based virus and the news flow reached its apex in mid-Oct with the S&P 500 bottoming on Oct 15, 2014, -5.6% from the initial outbreak, the 10 days after the market rallied 6.4%. During that period 10Y yields fell 100bp from 2.6% to 1.6%.

Lastly, in 2015 during the MERS outbreak, the news flow peaked out in mid-June 2015, while the S&P 500 troughed about a week earlier on June 8th 2015, -2.3% from the initial break out. The 10 days post the S&P rallied 2.1% and the 10Y actually peaked at 2.4% in parallel with the S&P's trough.

With economic activity disrupted and capital markets dislocated, investors are debating if Covid-19 will derail the global cycle. In times of sharp drops in asset markets, pessimistic prognoses are easy to make, but it is at times like this when some perspective is warranted. Coming into the year, we had a growing body of evidence that, after a tough 18 months, the global economy was on the mend.

The outbreak of Covid-19 has certainly changed the near-term narrative. It is an untimely shock, considering that the starting point of global growth was weak, and the recovery was very nascent. The disruptions to economic activity will create a pronounced impact on global growth in 1Q20.

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The question is whether this is an exogenous, transitory shock or one that fundamentally challenges the cycle. I am in the former camp. Indeed, throughout this expansion cycle, we have had a series of shocks to the global economy, which have led to a number of mini-cycles in global growth, but have actually helped to extend the cycle as we did not have the runway to go into a traditional overheating situation.

Given the uncertainty over the virus outbreak, I believe we will follow this Scenario.
Escalation in new geographies, disruption extends into 2Q20: New cases continue to rise in other parts of the world, before peaking by end- May. The disruption extends into 2Q20, affecting corporate profitability in select sectors, risking the emergence of corporate credit risks. If the dislocations in asset markets also persist into 2Q20, the sharp tightening in financial conditions may well become the overwhelming factor and exacerbate the impact on growth via weaker corporate confidence and capex and cutbacks in hiring activity.

In response, policy-makers around the world will step up easing measures – with fiscal policy in Asia and Europe and monetary policy in the US doing the heavy lifting.

I would expect the US Federal Reserve to cut rates and the RBA in Australian cut rate by 25bpts, along with other Reserve Banks.

On the positive side defensive assets have performed and bond yields have fallen to all-time lows. The Australian dollar has broken outside of the bottom of the range and is trading below 0.6500, provide a buffer to the RBA and Australian growth.

This pull back in market provides an opportunity for diversified portfolio's to make tactical assets allocation changes. I will be making contact over the next week to this end.

Should have any questions do not hesitate to contact me.

Summary of Major share indices

Index	1 Month	52 Weeks	YTD
DJIA	-10.07%	-2.37%	-10.96%
Nasdaq	-6.38%	+12.80%	-4.25%
S&P 500	-8.41%	+5.37%	-8.56%
Russel 2000	-8.53%	-7.12%	-11.51%
Europe 600 Index	-8.54%	+0.38%	-9.66%
UK FTSE 100 Index	-9.68%	-7.40%	-12.75%
Hong Kong Hang Seng	-0.69%	-9.31%	-7.31%
Japan Nikkei 225	-8.89%	-2.13%	-10.63%
China Shanghai Composite	-3.23%	-3.80%	-5.57%
ASX 200 (Australia)	-7.69%	+8.64%	-3.08%

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Australian Dollar

	Close	52 week Range
AUD	0.6483%	0.6463-0.7206%

Government Bonds

	Close	52 week Range
US 3 Month	1.295%	1.264-2.487%
US 10 Years	1.156%	1.099 – 2.770%
US 30 Years	1.679%	1.637 - 3.136%
Australia 10 years	0.708%	0.698-2.218%

Source: Wall Street Journal.

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