Global Thematic Investors' Diary

Iain Little and Bruce Albrecht, 18th March, 2020

Reduce/ re-orientate equities, raise cash, favour USD, EUR and CHF

Following our last Update on 4th March, we propose to lighten equities in portfolios and to re-orientate equity exposure towards the emerging winners in a changing world. The cure is proving worse than the disease.

The Coronavirus crisis, the most serious event since the Global Financial Crisis ("GFC") of 2008/2009, has set in motion a series of governmental policies whose unfortunate effect is to choke both demand and supply in the global economy. These policies - prudential measures taken by governments united in their desire to appear to be "doing something"- are likely to be worse, economically speaking, than the disease itself. Relief comes only with the passing of time or the finding of an anti-viral remedy, the latter a distant prospect at this stage.

Earnings news, monetary news, fiscal news and pandemic news are all following the disheartening course that we feared. An emergency Fed meeting last Sunday, slashing rates to near zero, failed to reassure. The next day, Wall Street produced the second of 2 record points drops in a week, falling **-13%**. Equity markets have fallen by an average of about **-30%** from their January highs.

Equity markets are now oversold and distorted by panic. The market finds it hard, if not impossible, to "price" risk when an end to the crisis is undefined and earnings unknown. And what discount rate should one use in a global panic when rates are near zero? Many stocks trade under "fair value" on "normalized" earnings. But the risks being taken by governments are such that there may be worse to come: bankruptcies in directly affected sectors like leisure, hospitality, airlines, hotels and "bricks and mortar" retail. There may even be nationalizations in troubled sectors. On the other hand, other sectors, also hit hard by the same waves of panic selling, may emerge as new long term leaders in a changing world where personal safety, health fears, de-personalizing technology and e-commerce may enjoy further and more widespread adoption.

In 5 years' time this crisis may be seen as a catalyst, an accelerator of trends and behaviours that were already happening over the last 10 years. More technology in commerce, more e-education, more care over health and hygiene issues, more remote working, more technology in communications, more de-personalized deliveries and trade. On the other side, fewer giant unprofitable airlines, fewer bricks and mortar start-ups, fewer restaurants, less globalization, less emphasis on communal activities. Our portfolios must reflect these trend and behavioural changes.

We therefore plan to

- *Reduce equity exposure to a level 30-35% below a client's personal strategic neutral*
- *Reduce in particular sectors vulnerable to the worsening economic situation*
- *Re-allocate reduced equity exposure to the new winners (healthcare, security, infrastructure, clean energy, e-Entertainment, e-Commerce or AI/ Robotics)*
- *Add to positions in gold after its fall*
- *Hold short term T Bills in USD (USD clients) or USD/ European currencies (for European clients) pending a return to the equity markets later in 2020*

A return towards strategic neutral will depend on the course of the Coronavirus pandemic and government policy. It is possible that we may have to react quickly in the event of good news, as markets are now very oversold. Investor sentiment can change quickly after a global panic like this.
