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Investment Report

March 2020

Strategy overview

The spread of coronavirus (Covid-19) has shaken global investment markets to their core. It is important to bear in mind that certain stock indices hit all-time highs in the third week of February. This was followed by the worst seven days for global stockmarkets since the 2008 financial crisis. As at the end of February, indices such as the SMI lost 7.40%, the S&P 500 8.20% and the Euro Stoxx 50 10.80% in value. The US index S&P 500 lost around USD 4,000 billion in market value within a single trading week. Gold and safe government bonds from the USA, Switzerland and Germany performed well during the February month under report, while their yields fell.

"The all-time highs posted by certain stock indices in the third week of February were followed by the worst seven days since the 2008 financial crisis."

S&P 500 Index

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There was, admittedly, a counter-movement at the beginning of March, when, amongst other things, a number of central banks also lowered their key interest rates. In the US, the Fed promptly cut its key interest rates by half a percent to between 1% and 1.25%. However, it is doubtful how much this will effectively achieve. The coronavirus is primarily causing a supply shock with interrupted output chains, and is only to a lesser degree constraining demand. So how are we responding to the current situation? At the fundamental level, when it comes to coronavirus, we are looking at the number of new infections. A steady decline in the number of infections outside China would indicate stabilisation, the opposite situation would support the pandemic scenario.

"The global economy is catching a cold."

On account of the direct and indirect effects of the coronavirus crisis, growth and earnings expectations will probably have to be revised further downwards. In our view, it is still too soon to be talking about a possible recession. Once again, it is important not to panic, to stick to the established investment style and to analyse the situation soberly. As mentioned in our last market assessment at the end of February on the topic of coronavirus, we are sticking to our credo of a broadly diversified asset allocation. Gold and selected government bonds act as portfolio stabilisers. We are currently giving the equity ratio a neutral weighting. We are considering raising this at a later date, when the situation has become clearer.

"The coronavirus crisis is demonstrating just how dependent the global economy is on China and on global supply chains."

In our view, an important consideration is the fact that the debate about an economic decoupling between China and above all the USA is likely to be stoked further – with the issue being driven by US President Donald Trump. In a recent interview, the distinguished economist Gabriel Felbermayr said that the virus could prove to be globalisation's "Lehman moment". Similarly, Peter Navarro, economic advisor to US President Trump, has called the Corona crisis a wake-up call that is drawing attention to America's dependence on China. Given these viewpoints, one should ask what risks and costs of different strategies we are prepared to bear. Do we want to benefit from attractive conditions with China as a supplier, but in return expose ourselves to the risk of becoming dependent and powerless? Or wouldn't it be better for us to invest in our own development, possibly lagging a little behind, but being able to rely on ourselves? These are the lessons to be learnt from the present crisis – politics and business are therefore called upon to act.

"The coronavirus should be a wake-up call for us to reduce our dependence on China."

Politics

Joe Biden's impressive win in the Democratic primary in South Carolina triggered a momentum that took the candidate himself by surprise. Having almost been pronounced dead in the water, the many wavering members of the party base and within the Democratic leadership suddenly found a consensus candidate behind whom they could rally. Joe Biden is now ahead of Bernie Sanders in the race to become the Democratic presidential candidate. The biggest losers on Super Tuesday were Elizabeth Warren and Mike Bloomberg. The latter had channelled around USD 600 million into his battle to be chosen as the presidential candidate, but has now abandoned his campaign. Pete Buttigieg and Amy Klobuchar have also pulled out of the race.

"Joe Biden – the comeback kid – experienced a real Super Tuesday."

It all boils down to a race between Joe Biden and Bernie Sanders. In our view, Joe Biden has the edge over Bernie Sanders. The Democrats will be selecting their presidential candidate at the National Convention in Milwaukee (Wisconsin) from 13 to 16 July 2020. From a Democratic perspective, it is important to avoid a so-called "contested convention". This is a nomination convention at which none of the candidates has the support of a majority of delegates. In such an event, delegates negotiate and vote until a majority has been achieved.

"From a Democratic perspective, a so-called contested convention is something to be avoided."

In addition to coronavirus, another uncertainty is certainly the outcome of the US election at the beginning of November. At present, the market is expecting Donald Trump to secure a second term. From the perspective of financial markets, the biggest negative surprise would be a win for Bernie Sanders with his very left-wing political agenda. His election victory would undoubtedly have the potential to trigger major market upsets. Sander's radical proposals for the American healthcare system, coupled with his threatened tax policies, would not be well received by investors.

"Please, not Sanders."

Economy

As mentioned above, financial markets were palpably unsettled by the coronavirus outbreak, regardless of the geographical location and the extent to which the virus directly impacted them. The extent and speed of the downturn took us by surprise too, but as is so often the case with financial markets, downward movements tend to be very fast and sudden. There is no doubt that the global economy is likely to suffer a setback in the first and probably in the second quarter as well. The OECD was the first to state that its baseline scenario was now looking at a downturn in growth of this order. The rating agency Standard & Poor's reduced its economic forecast for the

"Downwards movements on financial markets often materialise very swiftly and abruptly."

Eurozone by a similar amount. The key question is whether the global economy will recover quickly from the coronavirus shock, and whether the second half of the year will see a real recouping of the previously lost growth component.

The next few weeks are likely to be crucial. If the spread of coronavirus can be contained around the rest of the world – as has been done in China, where the number of newly infected people is declining significantly – a so-called V-recovery is indeed likely to materialise. In other words: The current steep upward curve of new coronavirus cases reported outside China should flatten out within three to four weeks, and the day-on-day rate of change is likely to decrease accordingly to reflect this assessment. If the virus is not brought under control within the foreseeable future, on the other hand, economic damage could assume substantial proportions and result in a veritable recession. State financial support for firms in difficulty, which would probably include many small enterprises, should help limit the economic damage. It is important to prevent companies going bankrupt or having to let their employees go. This is where states will need to be proactive.

“V-shaped recovery versus recession.”

Equity markets

A look at corporate figures for the past quarter shows that their results proved to be better than expected. Once again, profit growth in America outstripped that in Europe – this is attributable to the fact that the majority of technology companies' profits came in ahead of expectations. At present, within a historical context, corporate earnings growth in 2020 are likely to come in below average. However, the benchmark year of 2019, when practically no earnings growth was recorded, is likely to be exceeded this year. Sectors that are less dependent on China are currently showing fewer risks of downside revisions by the analysts' consensus in respect of the 2020 earnings outlook.

“At present, within a historical context, corporate earnings growth in 2020 are likely to come in below average.”

Bond markets

G7 finance ministers and central bank governors held a telephone conference on 3 March. On this occasion, the participants reaffirmed their commitment “to use all appropriate policy instruments to achieve strong, sustainable growth and to guard against downside risks”. No specific measures are identifiable in this statement, however. Completely unexpectedly, only two hours later, the US Federal Reserve cut its base rate by 50 basis points. For the first time since October 2008, the US Federal Reserve announced a base rate cut outside the normal rhythm of its meetings. The unanimous decision

“Commitment to use all appropriate policy instruments to achieve strong, sustainable growth and to guard against downside risks.”

was justified by the impending economic impact of the new coronavirus. Financial markets had not been expecting the Fed to lower interest rates until the next regular meeting in two weeks' time. The measure has now been brought forward, which could send out a tricky signal. It is difficult to avoid the impression that the currency watchdogs are panicking. It is otherwise difficult to explain the urgent interest rate cut.

Although the measure may be welcomed by investors, it is not without its problems. For the American economy does not appear to be in any serious distress at present. In its brief statement, the Fed also wrote that the fundamentals for the domestic economy remain strong. There is no doubt that the global economy will lose momentum on account of the coronavirus outbreak. However, because of its huge domestic market, the American economy is much less vulnerable to a slowdown in the global economy than other industrialised countries. The Fed is the only major central bank that still has some room for manoeuvre with its interest rate policies. Following this sizeable interest rate hike, however, the room for manoeuvre has become much smaller. Base rates, for example, lie between 1% and 1.25%. In contrast to the central banks of the Eurozone, Switzerland or Japan, the Fed has always made it clear that it would not consider lowering its base rate below zero. Within this context, this prompts the question of whether it would not have been wiser to keep the existing powder dry and refrain from taking a preventive interest move.

"The question arises whether it would not have been wiser for the Fed to keep its powder dry in terms of interest rate cuts."

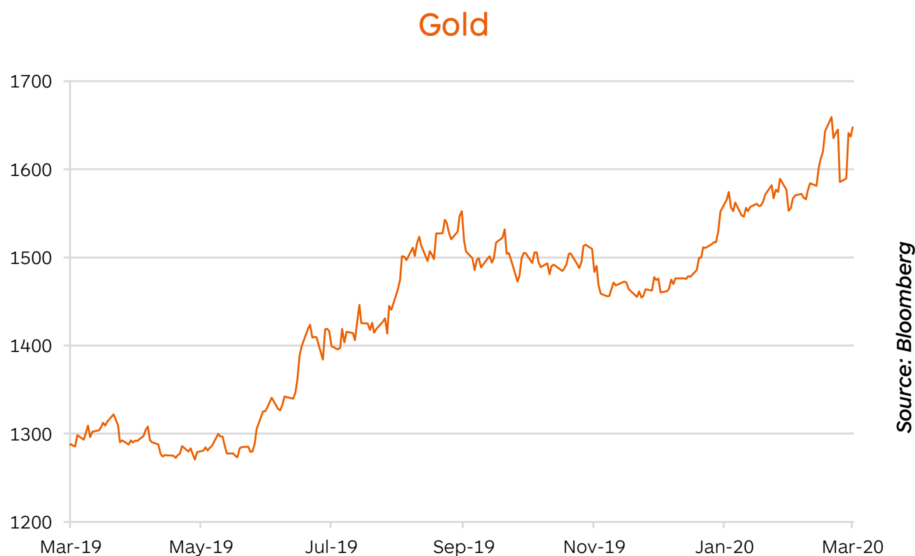
Through its measure the Fed is looking to calm jittery nerves – although it could also have the opposite effect. It may also be asked why was it not possible for the Fed to wait another two weeks before lowering rates? Is the situation really so dire that the easing of monetary policy could not be postponed any longer? And does the Fed perhaps know more about the threat to the American economy than has been communicated so far? All these questions are unlikely to calm public nerves. Instead, people in the USA are now likely to be even more worried than they were before.

"Through its measure the Fed is looking to calm jittery nerves – although it could also have the opposite effect."

Commodities

The price of gold has benefited massively from coronavirus fever. At its peak it rose to USD 1,690 per troy ounce, its highest level in seven years. The precious metal was not quite able to maintain this level, however. After a short-lived but noticeable correction, the price of gold held steady at around USD 1,650 per troy ounce at the beginning of March. In the interim, though, most stockmarkets have subsequently recovered somewhat.

"The gold price in coronavirus fever."



Between January and 5 March, the price of the precious metal rose by some 8.5%. Over the past eight months, the precious metal has gained almost 30% in value, and since August 2018 it has risen almost 40%. A particularly worrisome aspect: The current price level is just 15% short of the previous record of USD 1,900.

"The Fed's interest rate cut is supporting the price of gold."

Of course, the worries linked to coronavirus represent a special effect that is in particular boosting demand for the yellow precious metal. However, there are also a number of arguments in favour of supporting the gold price once the Covid 19 issue has been overcome. The first and foremost argument is interest rates. Since gold does not generate any current earnings, the lower the returns that can be generated elsewhere, the more attractive it is for investors. As is well known, these have long been negative for government bonds in several countries such as Switzerland or Germany, even when it comes to long maturities. But even in the USA, where nominal yields are still positive, they are sliding into negative territory when inflation is taken into account, for example in the ten-year range. A further easing of monetary policy by central banks is therefore likely at present. Geopolitical risks, which have receded into the background due to the coronavirus pandemic, may also support the price of gold. A weaker US dollar would also give the price of gold an additional boost. All these factors mean that the price of gold is unlikely to plunge once again when the coronavirus topic is no longer a price-driving topic. Instead, they are likely to push it towards new record levels.

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Currencies

As has been mentioned on numerous occasions in earlier Investment Reports, the Swiss franc is a safe haven currency. Within this context, the Swiss National Bank is facing a conundrum. For the SNB, the level of EUR/CHF 1.06 recorded at the end of February 2017 is likely to be the test. Greater intervention than in the past will probably be necessary to prevent the euro slipping yet again against the Swiss franc. From the technical chart and psychological level of 1.15 to 1.10, the decline is practically the same in percentage terms as that from 1.10 to 1.06. This means market analysts could target the 1.02 level if the SNB does not build up its defences against the depreciation of the euro.

"The Swiss National Bank will be forced to make further interventions."

Market Overview 28 February 2020

Stock indices (in local currency)	Current	1 Mt (%)	YtD (%)
SMI	9,831.03	-7.50	-7.40
SPI	11,897.75	-7.56	-7.32
Euro Stoxx 50	3,329.49	-8.43	-10.83
Dow Jones	25,409.36	-9.75	-10.55
S&P 500	2,954.22	-8.23	-8.27
Nasdaq	8,567.37	-6.22	-4.31
Nikkei 225	21,142.96	-8.82	-10.56
MSCI Emerging Markets	1,005.52	-5.26	-9.68
Commodities			
Gold (USD/fine ounce)	1,585.69	-0.22	4.51
WTI oil (USD/barrel)	44.76	-13.19	-26.70
Bond markets			
US Treasury Bonds 10Y (USD)	1.15	-0.36	-0.77
Swiss Government 10Y (CHF)	-0.82	-0.09	-0.35
German Bund 10Y (EUR)	-0.61	-0.17	-0.42
Currencies			
EUR/CHF	1.06	-0.40	-1.94
USD/CHF	0.96	0.16	-0.18
EUR/USD	1.10	-0.60	-1.67
GBP/CHF	1.24	-2.74	-3.54
JPY/CHF	0.89	0.46	0.25
JPY/USD	0.01	0.24	0.49

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