COVID-19 and markets: Your questions answered

UBS House View - Weekly Global

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Key Messages
Virus spread consistent with our central scenario.
Last week saw more positive signs that the spread of the virus is plateauing in parts of Europe. Even with increased testing, the number of daily new cases of the virus in Italy fell below 5,000—a level last reached on 23 March—for six consecutive days. The nation also registered its lowest daily death count in 2.5 weeks, and the toll in France and Spain is also retreating, while New York City registered a decline in daily deaths on 5 April. Nevertheless, President Donald Trump’s warning that COVID-19 could lead to up to 240,000 US deaths added to volatility in financial markets. In spite of heightened worries about the impact of the virus, in our central scenario we believe the imposition of lockdown measures will mean new virus cases peak in early April in Europe and by mid-April in the US; with the most severe restrictions lifted from May; and a coordinated monetary and fiscal response allowing for a subdued (U-shaped) recovery to take hold from the third quarter of this year. If we are proven right in our central scenario, we see the best risk-reward in credit, which in our view is closer to pricing in our downside scenario. This includes exposure to US high yield credit, which received an additional boost this week from a jump in oil prices following reports of a production agreement between Russia and Saudi Arabia. Equities look closer to pricing in our central scenario, so we recommend being selective in the space—seeing opportunity in oversold stocks in the US and Europe and resilient quality stocks globally, including select consumer staple and healthcare companies.

Takeaway: We see better opportunities in credit than most other asset classes, while also recommending being selective within equities.

Policy measures support the case for lower for longer.
Policymakers continue to take unprecedented measures to combat the economic slowdown from the coronavirus. In fiscal policy measures, Japan’s government has proposed a JPY 60tr (USD 555bn) package, equivalent to more than 10% of GDP. President Trump has called for an additional USD 2tr of spending on infrastructure, in addition to the USD 2tr fiscal stimulus

Week Ahead
1. Are governments bending the curve on COVID-19? Markets have largely focused on the headline data on the rise in total confirmed cases. But this metric partly reflects how widely nations are testing for the virus. We will be looking at a wider range of indicators—including the ratio of positive to negative tests, hospitalization rates, and the daily number of deaths—which collectively provide a more accurate measure of how far governments are curbing the contagion. Progress on these fronts could help lift markets.

2. Is stimulus working? Policymakers have launched a wide range of support packages, and more may come this week. Equally important, however, will be whether this stimulus-money is reaching its target quickly to limit job losses and bankruptcies. Bank lending figures and credit card usage data should help gauge the impact on the economy, as should surveys from companies on plans to furlough or let go workers. US initial jobless claims figures—which just registered a weekly print of 6.6 million—are released every Thursday, and will help investors evaluate US labor market conditions.

3. Will the US Federal Reserve prevent financial conditions from tightening? A shortage of US dollars

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package already agreed. Meanwhile, France is calling for the establishment of an EU fund to help member nations through the coronavirus crisis. To help keep financing costs low and ensure the proper functioning of markets, central banks have rolled out their global financial crisis playbooks in a matter of days—with the US Federal Reserve buying assets of USD 1.5tr since announcing a return to quantitative easing. Although global stock markets ended the week down 2.6%, policymakers continue to act with unprecedented speed and scale, and we think that ultimately their efforts will help avoid a global financial-crisis-style credit crunch. That said, further down the road, once the global economy recovers, all of the deficit-financed spending could lead to some inflationary pressure. Rising inflation expectations should, in turn, help Treasury Inflation-Protected Securities (TIPS) perform better than nominal Treasuries. And with rates set to stay lower for longer, we advise that investors improve their yield by considering emerging market US dollar-denominated sovereign bonds to their portfolios. There is also a higher yield available from put-writing strategies for investors who can implement options given current high volatility.

Takeaway: With a lower-for-longer environment set to stay, we recommend improving the yield in your portfolio.

Post-pandemic: What will change?
Many of the changes to our everyday lives will hopefully be relatively short-lived. But the COVID-19 pandemic will also, in our view, accelerate some longer-term trends as we have seen over the past months. Virtual care provider Teladoc reported an unprecedented 50% rise in daily visit volumes in the US for the second week of March. Telemedicine can offer access to routine medical care without risking exposure to additional health risks or further straining hospitals, and has the potential to lower the cost of care by shifting treatment away from expensive hospital locations—supporting the longer-term trend in Healthtech. It also only took scientists less than 30 days to sequence COVID-19—showing the potential in genetic therapies. As we continue to stay at home, the lessons from social distancing are likely to persist. Amazon ramped up hiring, adding 100,000 new roles to deal with heightened demand, further demonstrating the potential of opportunities in the digital transformation space, including e-commerce and fintech. Staying at home has also accelerated the revolution in food—US grocery delivery service Instacart had to put in an 80-order daily cap to deal with rising demand.

Takeaway: The pandemic will accelerate some longer-term trends, and investors can buy into secular winners at a discount given global stock markets are still over 25% off their highs.
Weekly Global

Deeper Dive

COVID-19 and markets: Your questions answered
by Global Chief Investment Officer Mark Haefele

In recent weeks, with the help of colleagues around the world, I have conducted a number of video calls to keep our clients informed of our investment views in the current fast changing circumstances. We try to answer as many of your questions as we can on the call. Here I have pulled together our replies to five of the most commonly asked questions.

Please also join us live on Tuesday, 7 April 2020 for our next livestream event when we will be taking a deeper dive into different asset classes. To watch the livestream on the day, click here. To add a reminder to your calendar, click here.

1. **When do you expect a rebound? Will it be gradual or sharp?**

In the near term, the path for economic growth and market performance will likely depend on how quickly economic activity can normalize following measures to contain the virus and how much policy responses can limit bankruptcies and job losses. We see three scenarios, of which the central one is the most likely outcome in our view:

- **Central scenario:** New cases reach a first peak in Europe by early April and in the US by mid-April. Severe restrictions to limit the spread will be lifted by mid-May. A second wave of infections with potentially higher case numbers means intermittent restrictions will remain in place for the rest of the year in Europe, the US and China. A coordinated monetary and fiscal response eventually provides the necessary funding to backstop affected businesses and industries, but it arrives too late to protect all. We expect a subdued U-shaped economic recovery from the third quarter into the first quarter of next year. By year-end, we would expect the S&P 500 to trade around 2,650.

- **Upside scenario:** The peak in daily new cases has already been reached in Europe and will peak in the US by early April. Measures to mitigate the spread will be gradually relaxed from May onward. Some restrictions will likely persist through 2020 in order to control a second wave of infections. Government stimulus is sufficient to avoid lasting damage to the economy, and allow growth to begin a V-shaped recovery in the third and fourth quarters. By year-end, we would expect the S&P 500 to trade around 2,900.

- **Downside scenario:** New cases continue to rise in Europe and the US into May or June. Restrictions remain in place into the summer and are re-imposed intermittently for the remainder of the year, as a second infection wave proves difficult to control in Europe, the US and China. Government policy is unable to meaningfully offset the lengthy demand shock, and economic growth would have an L-shaped profile through 2020. We would expect the S&P 500 to trade around 2,100 by year end.

2. **Have we seen the trough in equity markets?**
It is difficult to say with any certainty whether the trough has been reached, even though markets have rebounded somewhat. As noted above, in the near term, market performance will likely depend on how quickly economic activity can normalize, and how much policy responses can limit bankruptcies and job losses. We can’t rule out our downside scenario which would likely result in further equity market losses. As a result, we favor taking risk in credit over equities, because the former is closer to pricing in our downside scenario. Within equities, we believe it is important to be selective after the recent rally and so are focusing on identifying oversold and resilient stocks and opportunities to buy into long-term secular trends at a discount. For those that are already invested, we advocate diversifying globally and across asset classes.

3. When is the best time to invest? Now or in three to six months?
With global stocks still in a bear market, long-term investors can put excess cash to work at discounted prices. Putting excess cash to work in a lump sum has the highest likelihood of success. But for investors worried about bad timing given market volatility, it is possible to use other strategies to build your portfolio. For investors who can implement options, high volatility means that the yield on put-writing strategies is higher. This strategy also allows a pre-commitment to investing during dip-buying opportunities, and it can also be combined with an averaging-in strategy, which enables investors to deploy capital over a set schedule, while smoothing near-term bumps. You can learn more on taking advantage of higher volatility here.

4. I am concerned about my retirement accounts. What impact will the pandemic have in the short and long term?
Sharp market declines—in 1Q the S&P 500 reached bear market territory in the fastest time on record—can leave some investors tempted to sell to avoid further potential losses. But policymakers have shown a willingness to act, and the virus has now been contained in China and shown some signs of slowing in Italy. This has lifted markets, and further upside cannot be ruled out, but neither can the downside. Downside risks can be better managed through diversification across assets and regions.

Over the longer term, it is important to remember that bear markets are painful, but also rare and relatively short-lived. Since WWII, during S&P 500 bear markets the maximum drawdown has been 34.5% on average, erasing 65 months of prior gains and taking 39 months to reach a new all time high.

To help overcome the behavioral bias to sell out at the wrong time, it’s important to build a robust financial plan. Investors must think carefully about how much to devote to short-term needs, while setting aside a sufficient amount to invest for the long term. We believe the Liquidity. Longevity. Legacy. approach* can help investors achieve their financial objectives, reduce their anxiety about short-term risks, and enable them to take advantage of longer-term opportunities. For example, by ensuring that you have sufficient resources in your liquidity portfolio, the need to sell assets with potentially high long-term returns to meet near-term cash requirements can be avoided.
5. What will have changed permanently once the coronavirus crisis is over?
Many of the changes to our everyday lives as a result of the coronavirus will hopefully be relatively short-lived. But the COVID-19 pandemic will also, in our view, accelerate some longer-term trends. Three areas stand out:

• Telemedicine can offer access to routine medical care without risking exposure to additional health risks or further straining hospitals. It also has the potential to lower the cost of care by shifting treatment away from expensive hospital locations, and to expand access to care for those in under-serviced communities. This underlines the opportunity in health technology.

• It took less than 30 days for scientists to sequence SARS-CoV-2, the virus that causes COVID-19, well below the five months it took to complete the genome sequencing of the SARS virus during the outbreak in 2002. The low cost of gene sequencing, as well as the availability of gene sequencing machines, likely aided researchers in their speedy replication. Genetic therapies in our view represent a paradigm shift in healthcare delivery.

• Lessons from social distancing are likely to persist, further boosting the growth of e-commerce and remote working. A more online lifestyle is also going require more investment in 5G infrastructure, creating investment opportunities in the digital transformation space. Staying at home has also accelerated the revolution of food—consumers are ordering food deliveries via mobile apps like Uber Eats—a trend that we expect to continue as consumer preferences shift and urbanization continues.

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* Timeframes may vary. Strategies are subject to individual client goals, objectives and suitability. This approach is not a promise or guarantee that wealth, or any financial results, can or will be achieved.
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