Review of Financial Markets Q1 2020

- The new decade began with one of the greatest human catastrophes in recent history. The coronavirus, which originated in China, gradually spread across the globe and brought large parts of the economy to a "standstill". The government measures taken for health reasons had a shock effect on both supply and demand and inevitably leads to a recession.
- The consequences for financial markets were extreme volatility and turbulence, with a flight to liquidity being one of the key drivers over recent weeks. This has led to indiscriminate selling across most asset classes and investment vehicles. Forced liquidations and extreme risk-averse behaviour reinforced the downward trend. Government bonds as a safe haven ultimately managed to regain territory. The big losers in fixed income were lower-quality high-yield bonds, especially those issued by US energy companies.
- The selling pressure in equity markets was at times pronounced to such an extent that trading was temporarily halted on some stock exchanges. The volatility of US markets skyrocketed, increasing approximately fivefold. The global index for equities lost around 20% during the first quarter. Emerging markets and small caps suffered even sharper losses, as did European equities, where the index was weighed down by the financial sector. On the other hand, equities in Switzerland, China, as well as the technology sector held up better than the broad market.
- Commodities were also caught in the same wave, with only Gold being able to post a small gain for the first quarter. The most striking development was the collapse of crude oil prices, losing over 60% in the wake of the dispute between Russia and OPEC over the continuation of production restrictions. The immediate consequences will have to be borne by producers, particularly in the US fracking industry, where production costs are above current market prices. The positive effect of lower prices on consumption is hardly to be felt at the moment amidst heavily reduced demand.
- Currency markets were in comparison relatively calm regarding main investment currencies. The US dollar was in high demand and generally stronger, with the British pound losing approximately 7%. The Swiss franc gained 2.5% vs. the Euro and is likely to have been held from appreciating further by interventions from the SNB. Currencies in commodity-heavy countries such as Brazil, South Africa or Russia lost around 20% in the first three months.
- Reactions of policymakers to the pandemic were mostly hesitant at first, but all the more drastic after in an effort to compensate. Central banks opened the floodgates to supply the markets with liquidity in order to ensure continued functionality, aiming to counteract insolvencies or at least achieve some level of stability of the process. To this end, in addition to interest rate cuts, quantitative easing measures introduced during the last crisis were reactivated with outright asset purchases from central banks.
- Government measures to support the economy have taken on new dimensions in their attempt to provide relief. The USA approved a USD 2 trillion package, which will increase the government deficit to around 15% of gross domestic product (GDP). Both Germany and Ja-

pan are stimulating their economies to the tune of around 10% of GDP, which is significantly more extensive than what was seen during the crisis of 2008/09. The package of measures to cushion the economic consequences in Switzerland amounts to around CHF 40 billion (5.8% of GDP), and more stimulus is being implemented around the globe. In contrast, measures in China are (currently) rather timid at around 3% of GDP and substantially lower compared to both other countries as well as the last crisis.

Where do we go from here?

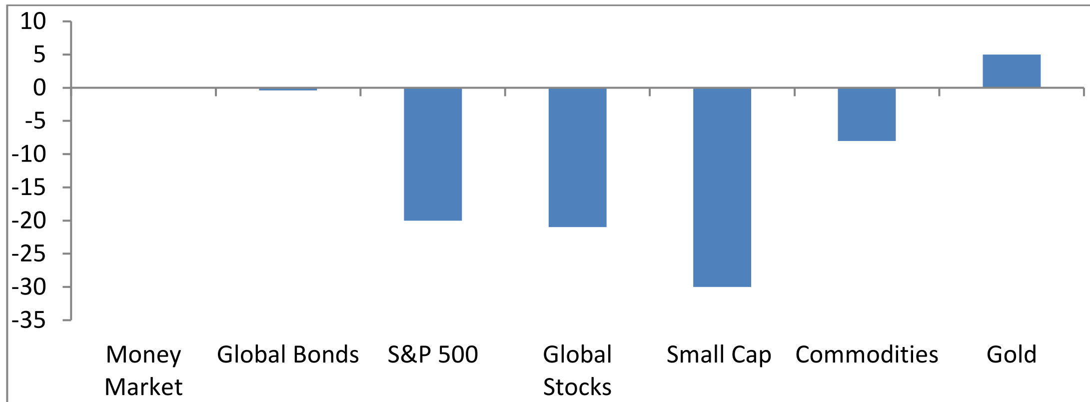
The extent of the economic damage depends on how long the quarantine conditions last, how quickly normalisation will take place and how efficient the government programmes are turning out to be. There are different developmental variants conceivable, which have different probabilities.

1. The pandemic is taking a course similar to that in China and to annual waves of influenza. The economic measures are sufficient and limit the collateral damage. Thus, the economic recovery that has already started to get under way in China will also gain momentum in other countries in the coming months. The global economic upswing is underway in the second half of the year. For financial markets, these prospects would be reassuring and the increased risk appetite of investors will provide a positive impulse, particularly for the stock markets.
2. There are hoped-for but not expected medical improvements, for example through successful trials of (combinations of) existing drugs to show efficacy with patients. A broad-based testing of the population for antiviruses will enable a quicker and more targeted reversal of shutdown measures. However, this must not be limited to individual countries, otherwise a partial blockade will remain in place. The development of a vaccine usually takes a long time, but the announcement of a shorter window of feasibility alone would be helpful. The prospect of taming the pandemic would considerably boost economic confidence and thus also become visible on the financial markets.
3. The pandemic cannot be tamed definitely and a second wave shakes society. The economy fails to get back on track and state aid packages are falling short. The plunge into a deep and prolonged recession becomes inevitable. Financial markets are under stress and the willingness to invest in risky assets is moving ever lower.

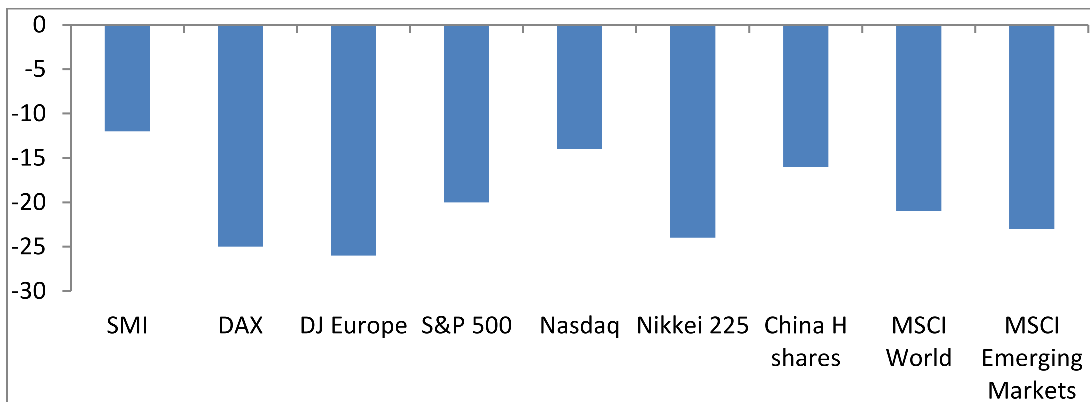
We assign the highest probability to the first scenario or that a similar variant of it will prevail, and hope that the global efforts of the pharmaceutical industry will yield encouraging results in order to accelerate the start of a return to normalcy. However, the possibility of an ongoing pandemic and the continuation of government-imposed restrictions and their detrimental effects on the economy cannot be neglected. For the time being, we believe a reasonable and sensible strategy is to hold our positioning and await further clarity by continuously monitoring developments around the coronavirus and economic data.

Wangs, 2 April 2020

Gross return 1st quarter 2020 in USD for different asset classes (in %)



Performance 1st quarter 2020 in local currency for selected stock indices (in %)



Wyss & Partner
Asset Management and
Investment Counseling AG

Bahnhofstrasse 17
7323 Wangs, Switzerland
P +41 81 720 06 88
F +41 81 720 06 89
info@wysspartner.ch
www.wysspartner.ch