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Markets Update

Following our last updates on Covid-19 on 24 February and 26 February here is a further market update to follow what is happening during this health crisis. Today equity markets are negative by between -3% to -8%, while bonds and gold are up between +1% to +2%.

The reason for larger negative moves in equities today (Eurostoxx50 -6%) is a combination of the continuing spread of the coronavirus, particularly in Italy which is placing the Lombardy region in quarantine, combined with a collapse in the OPEC+ talks late on Friday. The latter resulted in Saudi Arabia announcing plans over the weekend to increase oil production to 10m barrels per day with sights on 12m a day in a direct challenge to Russia. The 14 OPEC countries had wanted to cut output by 1.5 million barrels a day, or about 1.5% of world production. OPEC countries like Saudi Arabia and Iran say they need non-member allies like Russia to take 500,000 barrels of that cut on themselves. A price war and supply glut has sent oil prices down by around 30% overnight and has destabilised equity markets.

So far, the new coronavirus has led to more than 100,000 illnesses and more than 3,000 deaths worldwide. This could be compared to the "flu", also called influenza. In the U.S. alone, the flu has caused an estimated 32 million illnesses, 310,000 hospitalisations and 18,000 deaths this season, according to the Centers for Disease Control and Prevention (CDC). Most of the time flu activity peaks between December and February, although activity can last as late as May.

The OPEC+ price war has come on top of equity market jitters over the seriousness of the coronavirus impact on the world economy. A fall in energy consumption due to reduced activity has already meant that oil prices were under pressure and in need of support so the disagreement between OPEC participants and Russia is most unwelcome. The good news being masked by all this is that China has passed 'peak infection' and the number of new virus cases has flatlined (see here). Indeed the Wuhan region is now reported to be largely back to work as the disease is reportedly now under control.

Straits Times: 09 MAR 20 - "***China closed several makeshift hospitals for coronavirus patients, some schools reopened and Disney resort staff went back to work on Monday (March 9) as normality slowly returns to the country after weeks battling the epidemic***."

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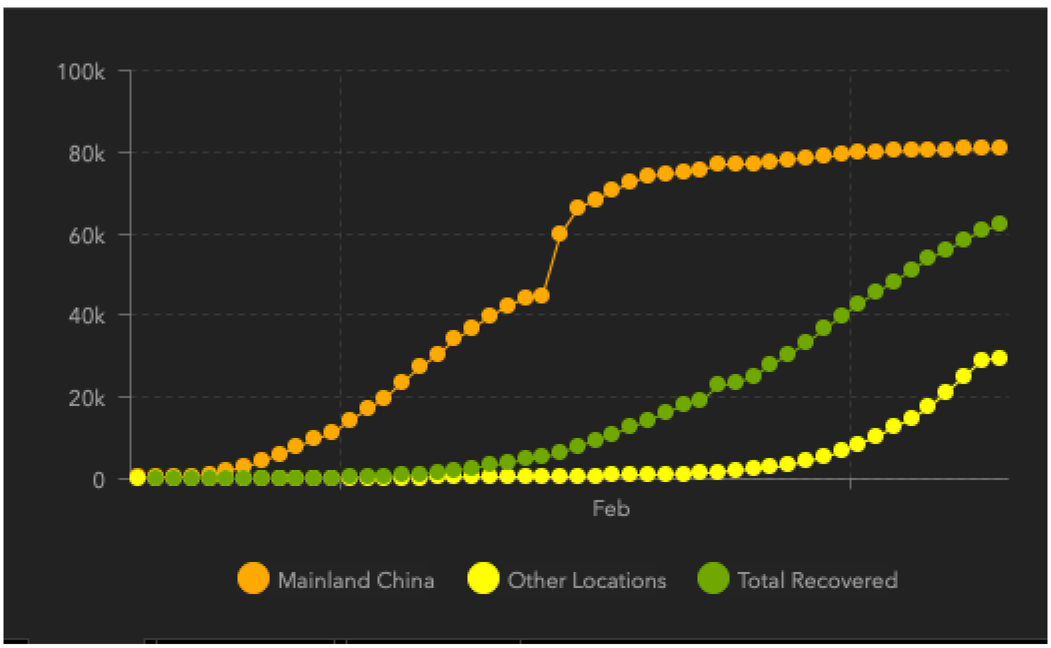
The focus now turns to Europe where the outbreak in northern Italy has surprised with significant new cases (7375 in total) and an elevated 4.96% fatality ratio (366 deaths). The spread of the virus from Italy into other countries and the lack of control measures by authorities are worrying and have the potential to slow the European economy for longer if stricter enforcement is not forthcoming in the short-term. The lockdown of the area around Milan is, however, the kind of action that is needed to make things better, as was demonstrated in Wuhan earlier this year.

The question is whether Europe can quickly reach 'peak infection' like China or if the spread of the virus cannot be effectively contained. For the most telling graph see the tracker of new cases in China and internationally and the total number of recovered patients, here:



COVID-19 - new cases in China, Internationally, and Total Recoveries

It's impossible to say if this health crisis will be worse than originally thought and we suggested that the first couple of months were likely to be very uncertain as nations learn how to handle the infection rates. It is likely that this will come under control as we go into Q2 as measures take effect and in the northern hemisphere air temperatures rise, which diminishes transmission rates. In the meantime, equities will remain under pressure and likely to overreact to the downside in the short term before regaining composure and forward-looking to an economic recovery later in the year.

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Gold, fixed income and cash are positive for the active model portfolios, and the European equity capital-protection is now effective. We are not selling equities at this level but are closely following the market developments. The key element this week is gauging the virus spread in Europe versus China at the same stage earlier this year and working out if governments are taking appropriate action to contain it.

Lorne Baring
Managing Director