MARKET INSIGHTS

from Ziegler Capital Management

Our View on the Coronavirus and the Stock Market

For over a week now, global stock markets have been reacting to the latest news reports of the new coronavirus. Like many, our equity teams have spent considerable time thinking through the cascade of “what happens if” scenarios. Most of us have lived through other pandemics to discover that in the end, the damage to the broader economy and stock markets is short term and recovery happens. Meanwhile, the media machine and talking heads are on the job to make sure everyone knows the coronavirus has arrived. The occasional reference to the early 1900’s and Spanish flu is the best example of how far it goes, with an estimate of over 500 million people infected. Could that happen again? Not likely, as our science and containment capabilities are very much advanced.

One issue that has been pointed out is the fact that the market is “high” and near peak levels this time around. Therefore, there is more room for a sell-off to occur, and the play through into technical factors could play a bigger role causing a self-fulfilling break down and even larger sell-off. The question we must ask ourselves is whether the highly contagious aspect of the virus will drive a higher economic contagion impact. We are already seeing the reaction to travel-related stocks and have seen stocks of companies most exposed to China moving much lower. Quantifying the impact would be impossible to know but for China we have seen an estimated impact to GDP in the range of 50 to 150 basis points. Not a disaster, but when we were all thinking that trade would get better, it does add to the risk of a global growth slowdown.

In client portfolios, we have reviewed all positions for exposure. In those instances where there is direct and high exposure to China, we have erred on the side of caution and reduced exposures. Some examples would include travel and leisure companies and companies with large end market exposure to mainland China. Similarly, companies with derivative exposure have also been evaluated and in some instances either sold or reduced in size. In all cases, we will be monitoring developments with an eye toward potential disruptions and additional portfolio changes. Likewise, we will be reviewing the situation for opportunities to participate when the risk/reward ratio turns favorable.

So what does an investor do? Those who are nimble, don't have tax issues, and can execute a meaningful cash raise have the potential to time the market, but that is always the case. The risk of selling and not being timely enough to get back in occurs when infection numbers reverse or just slow, and the market experiences a swift snap back. We don't want to diminish the human impact and suffering that has already occurred with more to come, but longer-term investors should take solace in the historical experience which tells us that pandemics are best described as a buying opportunity.

We are hopeful that medical science will leverage its already amazing progress and execute a safe and effective response. For that we are bullish.

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