Key Perspectives from Canada's Largest Asset Managers About the Coronavirus Crisis

February 27, 2020

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Coronavirus-related fears have rattled markets and have resulted in plenty of advisor inquiries about the state of the investment landscape. We are product and portfolio construction experts, but when it comes to the economic and market-related ramifications of situations like this, we like to defer to our fund company partners, many of which have experts around the globe monitoring things. To that end, we have sought out recent commentaries about the coronavirus crisis from these partners and we highlight some of the key perspectives in this piece.

To quickly review, the S&P 500 shed 6.6% from Monday to Wednesday this week, in local currency terms, while the S&P/TSX slipped 4.5% over the same time frame. Investors piled into the safety of government bonds, pushing North American long term yields to levels never seen before in some cases. The CBOE Volatility Index, or VIX, briefly exceeded 30 on Tuesday – a level that has rarely been seen since the financial crisis. The VIX is a measure of implied option volatility for S&P 500 index options and it is often seen as a gauge for the amount of fear in the market.

We would like to remind readers of previous epidemics and their effect on the stock market. Looking back 40 years, previous epidemics have all led to the S&P 500 increasing in value over the six months after the virus was discovered, except for the HIV/AIDS epidemic in 1981. Even then, the decline was minimal. Over 12 months, there were only two instances of the market declining after the disease was discovered. There is a possibility that the coronavirus impacts the global economy more than previous epidemics, however, the stock market's track record of a quick recovery from these events can be reassuring.

Chart 1: Epidemics and Stock Market Reactions

Epidemic	Month End	6-month % change (USD) of S&P 500	12-month % change (USD) of S&P 500
HIV/AIDS	June 1981	-0.2%	-10.7%
Pneumonic Plague	Sept 1994	8.2%	26.3%
SARS	April 2003	14.6%	20.8%
Avian flu	June 2006	11.7%	18.4%
Dengue Fever	Sept 2006	6.4%	14.3%
Swine Flu	April 2009	18.7%	36.0%
Cholera	Nov 2010	14.0%	5.6%
MERS	May 2013	10.7%	18.0%
Ebola	March 2014	5.3%	10.4%
Measles/Rubeola	Dec 2014	0.2%	-0.7%
Zika	Jan 2016	12.0%	17.5%
Measles/Rubeola	June 2019	9.8%	N/A

Source: Dow Jones Market Data

Before sharing the commentary from our product partners, we invite readers to apply a bit of perspective when reading headlines about the magnitude of the point decline of major stock benchmarks. The 1,000 point slide in the Dow Jones Industrial Average certainly was prominently featured in the press, but that (only) marked a 3.6% decline. By comparison, the benchmark's 508 plummet during Black Monday in October of 1987 was an astounding 22.6% of its value. This probably does little to heal the wounds from the recent market drawdown, but perspective does matter here.

BMO Global Asset Management (Brian Belski, Investment Strategist)

- "While U.S. stocks have largely shrugged off coronavirus fears in recent weeks, concerns appear to have shifted to first quarter earnings season with many investors suggesting the outbreak will have a detrimental effect on the bottom lines of S&P 500 companies. While this outcome cannot be completely ruled out, we are just not seeing the tell-tale signs (i.e., excessive negative guidance, significant EPS cuts) at the moment to suggest a deterioration of the earnings environment is imminent, in our view. In fact, we believe there are still too many unknowns to determine precisely what any eventual impact would have on U.S. stocks, regardless of what is being talked about in the media. Nonetheless, there is no doubt that specific areas of the market are being notably impacted by this outbreak. However, even for these companies, the longer-term fundamental outlooks have largely remained intact, based on our work. Therefore, while the coronavirus certainly warrants persistent monitoring in the coming months, we do not believe investors should be pressing the panic button just yet."

Capital Group (Jared Franz, Economist)

- "Assuming the outbreak is contained soon, it's likely global economic growth will experience a V-shaped recovery characterized by slower growth in the first half and a significant acceleration in the second half of the year. The U.S. economy will probably follow the same course. U.S. economic fundamentals remain sound, labour markets are resilient and the Federal Reserve stands ready to take action as needed. The coronavirus looks to be a modest but temporary restraint on U.S. economic activity via secondary channels of impact, but should not derail my growth expectations of roughly 2% in 2020."

Dynamic Funds (Myles Zyblock, Chief Investment Strategist)

- "(Monday)'s decline in share prices was one of the more severe sell-offs seen over the past decade. If history rhymes, we'd expect to see some near-term stabilization in the performance of equity markets. Yet, subsequent calm in the markets could prove short lived. Investors are now squarely focused on the risk that COVID-19 is spreading internationally.

Fresh outbreaks in Italy, Korea, and Iran have placed the spotlight on the fact that this is no longer a China-centric issue. And, with this comes a potentially new and more disruptive phase for the global economy and corporate earnings. The ability of these countries to contain the spread will become the next important focal point for investors.

We are closely monitoring the case numbers and will report on any important changes. This is a highly unpredictable situation and, as we have said on numerous occasions in the past, proper portfolio diversification is the best tool an investor has to handle future uncertainty. The large bond market rally can just as quickly turn into a nasty sell off, and the inverse goes for equities. But, having sufficient exposure to both asset classes ensures a better ride for an investment portfolio through time. Diversification - or the mixture of low correlated asset classes - removes the need for forecasting, which is proven to be largely ineffective anyways."

Fidelity Investments (Bruce MacDonald, Portfolio Manager, and Eileen Dibb, Portfolio Manager)

- "The extent of damage due to coronavirus outbreak is hard to predict at a time when number of cases continue to rise, but rapid medical and monetary policy response from the Chinese authorities is encouraging. If contained, the economic impact of this outbreak will be limited, and some recovery can be expected as soon as in the second quarter of the calendar year 2020. While the outlook for individual companies and sectors may be affected to varying degrees, our positive medium-term assessment of Asian equities on the back of demographic trends should remain intact. That being said, the probability that the global economy is entering late cycle has increased and this will also help inform our investment decisions going forward."

Invesco (Kristina Hooper, Global Market Strategist)

- "We continue to receive information indicating that businesses are being impacted. This is a classic exogenous shock. Flash PMIs for a variety of countries are showing a coronavirus-related deterioration. And more companies are warning that earnings will be negatively impacted by the COVID-19 outbreak. In this environment, it is easy for investors to panic. Following are a few things for investors to remind themselves of:

o The 10-year Treasury does not have medical training. In other words, I am taking its yield drop and any resulting yield curve inversion with a grain of salt because the economic impact all depends on the lifespan of the contagion. I am concerned about the recent reports of rising infection rates and serious infections among otherwise healthy people. However, I still hold out hope that this contagion will be short-lived, echoing the views of International Monetary Fund Managing Director Kristalina Georgieva, who said last week that it's too soon to make medical projections, but "we are still hoping that the impact will be a V-shaped curve" with a sharp decline in China and sharp rebound after the containment of the virus.

o Policymakers will be as supportive as possible, and supportive policy can supersede decelerating growth in dictating the direction of risk assets. China has provided very significant stimulus, both fiscal and monetary, and is poised to provide more. And last week Federal Reserve (Fed) Chair Jay Powell made it clear that the Fed will "closely monitor" the situation, which I believe means it is ready and willing to offer "insurance cuts" if need be, just as it did last year as a preventive measure to stave off the negative economic effects of the U.S.-China trade war. This should soften the drop, at least slightly, and certainly encourage a more robust rebound.

o The situation in China is already starting to improve. Infections have slowed. More factories are coming on-line. The work resumption rate is rising. It will take time to get back to full capacity, but in China the situation has been moving in the right direction. Hooper is following recession indicators closely, recognizing the potential need to make tactical shifts in portfolios with shorter-term time horizons if compelling signs of a recession appear. She will be vigilant in terms of watching for signs that the slowdown turns into a recession. Presently, she expects the economic expansion to continue, albeit more slowly."

Manulife Asset Management (Philip Petursson, Chief Investment Strategist)

- "Overall, we would suggest that from an economic perspective the coronavirus is likely to be disruptive to growth, but not destructive to growth. As such, the economic impact may likely lead to weaker earnings growth in Asian markets, with some spillover to U.S. equities through the first half of 2020. We expect this to be followed by an economic and earnings rebound as we have seen in the past. We would not suggest a shift in one's asset allocation merely in response to the current epidemic as we believe a recovery will follow in short order. For the time being, we continue to focus on the fundamentals and remain mindful of current equity valuations while looking for signals of a more meaningful earnings rebound in equities."

National Bank (CIO Office)

- "Just as data from China was indicating a stabilization in the number of new cases following extensive containment measures — prompting equity markets to rise earlier in February — the sudden rise of infected people in Italy, South Korea, and Iran revived fears of a widespread pandemic. Combined with last Friday's weak U.S. manufacturing and services economic figures, this was the perfect recipe to trigger risk aversion.

  We remain optimistic about global growth in 2020 whereas the bulk of what will inevitably be lost in terms of growth in Q1 should be recouped in the following quarters, likely helped by further monetary and fiscal accommodation. That said, the near-term outlook for equity markets has undeniably become more clouded in light of these new coronavirus cases springing up outside of China. As such, we will continue to monitor the situation closely in the coming days as new data allows for a better-informed assessment of the current situation, and we stand ready to readjust our asset allocation accordingly."

RBC Global Asset Management (Krystyne Manzer, Vice President, Portfolio Specialist)

- "Our view remains that from an economic perspective, the disruption should be minimal. We are now forecasting global economic growth of 2.9% versus 3.3%, so a 0.4% hit to annualized growth. While not negligible, at this time these expectations are mostly though not entirely attributable to the damage to China's economy rather than expectations of a prolonged or deepening hit to global economies. That said, we remain watchful for further signs of contagion. The economic backdrop has shifted to a more mixed picture from earlier this year after negative impacts from the U.S. government shutdown and China's economic slowdown receded. Added to the mix were the new positive forces of a potentially rising economic speed limit and supportive governments and central banks. The balance of these suggests that the trajectory for global GDP is not all that bad, and the team has raised their growth expectations slightly as a result.

  From a long-term perspective, it's important to recognize that virtually every year comes with its own set of economic, financial, or political events that give investors a reason to remain on the sidelines. The spread of the COVID-19 virus is one of these such events and we remain vigilant for signs of further escalation of the situation and its potential impact to the global economy. While these types of negative shocks almost always lead to weakness in risk assets, equity markets have in the past been resilient and ultimately remained on an upward course over a longer time-horizon. The one thing we know for sure is that the future is uncertain, but investors can benefit from financial markets by investing early, maintaining a long-term perspective and staying invested particularly when invested in a well-diversified portfolio."

TD Asset Management (Robert Vanderhooft, Chief Investment Officer)

- "There is no question that the outbreak will have negative economic consequences. Factory work has stalled, flights grounded, and supply chains disrupted. The virus will likely lead to downgraded economic forecasts, with some economies experiencing negative growth in the first quarter of 2020, and possibly into the second. We have no definitive way to estimate the extent of the economic damage, but feel that conditions for a U.S. recession remain low given strong corporate health, low unemployment, a relatively high savings rate, and strong consumer spending. The degree of impact to economies will vary however, as governments and central banks have different abilities to respond.

Notably, recession fears have not worked their way meaningfully into the bond market. Reaction in credit has been limited, even as coronavirus infections spread. Investment grade and high yield debt are holding at low levels with spreads remaining tight, keeping corporate borrowing costs near 30-year lows.

While we have a constructive view to the long-term, near-term we may see investors de-risk some assets, as growth factors remain uncertain and under pressure. While it is a continuing risk, and not our base case, a meaningful market correction could bring equity valuations down to more attractive levels. This can provide opportunities to increase exposures to high quality companies, that in our view will be higher than current levels in 18 months.

Without a doubt, disruptions are being felt in overall global business activity and financial risks may continue to mount over the next two quarters. However, if history is a guide, pandemic containment can be followed by a strong recovery in economic activity. Given continued supportive global monetary and fiscal policies, we believe the overall growth trajectory remains largely unchanged over a 12 to 18-month time horizon."

The Bottom Line:

The coronavirus outbreak has made a huge impact on global markets in recent days as the epidemic poses a gigantic risk to economies around the world. The viewpoints somewhat differ, but the common thread amongst our partners is generally the same: longer-term outlooks remain intact and there is cautious optimism for global capital markets based on a recovery from this current epidemic. As we go through these types of negative shocks, it is a great time to remind investors of the resiliency of equity markets in the past and the benefits of having a long-term perspective. The coronavirus outbreak is a highly unpredictable situation and the best way to handle the uncertainty for investors alike is to have a diversified portfolio to handle these inevitable bouts of volatility.

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(20-0341) 02/20