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INVESTMENTS

MARKET UPDATE: MARKETS FALL DESPITE CENTRAL BANK MEASURES

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The market turbulence in reaction to the coronavirus is showing no sign of easing, and the measures taken to manage both the spread and the economic impact are getting more extreme.

Yesterday evening, the Federal Reserve (US central bank) lowered interest rates to zero, its second emergency cut since the crisis began. The Fed also announced an increase to its bond buying programme- known as quantitative easing- and a range of other measures designed to ensure that the financial system continues to function through these uncertain times. With much of Europe locked down to control the spread of the virus, we are entering a period where the impact on economic activity will be severe for a time.

What started as disruption to supply chains due to the slowdown in China has shifted to concerns about falling demand as workers are told to stay home and shops close. This phase should pass, and fears should ease as the rate of new cases in badly affected countries like Italy peaks.

Markets were underwhelmed by the Federal Reserve's decision on Sunday. Investors had been expecting a coordinated response from governments across a number of countries- not just increased public spending but also measures to directly support the hardest-hit parts of the economy. Keeping smaller businesses operating during the disruption is key to the recovery.

The epicentre of the pandemic has shifted to Europe and away from China, where the rate of new cases has slowed to a trickle. Economic activity in the country is gradually increasing, and some businesses have restarted production, even in Wuhan where the virus originated.

We have been monitoring the return to work in China using various sources. It is difficult to get a full picture as any official data published by the Chinese authorities is treated with scepticism, but activity is picking up. During the lockdown in China, pollution over cities fell, but it is rising again now that restrictions are ending. Similarly, by keeping track of mobile phone data Baidu can demonstrate the Chinese are returning to cities.

As China goes back to work, the pressure on supply chains will ease. The country contributes so much to growth that any return to pre-crisis levels of activity would help to boost the global economy, even as other regions temporarily shut down. A combination of government support and a peak in new cases would help investors estimate how the virus may affect other countries and reduce the fear element driving markets at present.

Today, the G7 (US, Italy, Japan, Canada, France, Germany and UK) holds a conference call to discuss their response to the virus. Investors will watch the outcome closely for signs of coordination or examples of support for business activity. It is difficult to say exactly when the disruption will end. However, if authorities do what they can to limit the economic and social damage, then a peak in daily cases may help the outlook improve. If the experience of China or South Korea can be replicated, the overall impact could be limited to the first half of 2020 with a much better second-half as activity bounces back.

Despite everything that has happened over the last couple of weeks, the message to clients remains the same- try not to make any knee jerk decisions when it comes to managing your portfolio. The coronavirus has rattled the markets, but the impact is likely to be temporary, and the benefits from the measures introduced by the authorities should last much longer. Investors typically get rewarded for staying invested through this kind of turbulence.

Diversification- the spreading of investments across different asset classes and regions- should offer added peace of mind. Bond holdings could help to offset some of the losses caused by the fall in the stock markets.

Toni Meadows - Chief Investment Officer, Omnis Investments

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