Valvest

Investment View – 2nd Quarter 2020

Review

An eventful half year in the financial markets is coming to an end. The crash in March was followed by an unprecedented market rally. While the central banks are widely credited for the latter event, we also see additional fundamental factors that come into play.

The financial markets first priced in a complete standstill of the economy with unknown duration. Coupled with a demanding valuation, this has led to an abrupt and sharp correction. However, it soon became apparent that the measures taken in several countries led to a flattening of the infection curve and hospital utilisation, and that mortality is lower than originally feared. Crisis scenarios such as those in Italy were largely avoided.

The expected duration of the lockdowns could thus be better estimated, which led to a calming of the markets. At the same time, governments and central banks took extensive measures to support the economy and consumers. Defaults and bankruptcies were thus averted for the time being. This has greatly increased the probability of a rapid economic recovery.

Looking at the market or at individual companies from a fundamental valuation perspective, the recovery of the markets is understandable. Although many companies will post declining sales and profits this year, they expect to return to growth at the end of the year. However, differences between the individual economic sectors could not be greater. Many companies in the technology and healthcare sectors will report sales and earnings growth this year, albeit lower than originally planned. Sectors such as industry, gastronomy or tourism, will have to cope with sharp declines in sales and profits.

Thanks to active asset management, we are able to adjust the positioning of our clients' portfolios to economic conditions at any time and by carefully selecting individual companies and sectors, avoid the hardest hit areas and thereby protecting the capital of our clients.

Outlook

The various consequences as well as the final course of the corona crisis are not yet foreseeable. The additional indebtedness of states and companies, a higher unemployment rate, rising input costs due to shifts in the global supply chain and increasing social unrest are already having a negative impact on the economy. On the positive side, a certain propensity to consume could arise, triggered by the forced deprivation during the state of emergency in recent months. In combination with the ongoing intervention by governments and central banks, this can have a considerable positive effect on economic development.

Even if economic development should stagnate, many high-quality companies generate attractive returns for their owners. In a long-term low interest rate environment, reliable returns and profit growth are of great value. Accordingly, investors are willing to pay a premium price for companies with these attributes.

Should the steady easing of lockdowns, protests or the presidential campaign lead to a second wave, which in turn requires a lockdown, a renewed market correction can be expected. As a result, government and central bank interventions would reach an additional escalation level. However, as governments are now better prepared to take immediate action in such a scenario, the likelihood of a second complete lockdown is significantly lower.

Investment policy

There are currently a large number of uncertainties. Deflationary developments coupled with inflationary interventions lead to risks in all asset classes, including cash. If the spread of the virus stabilizes at the current level, the stock market can focus on future earnings again and is still attractive compared to other asset classes due to its yield premium. Participating as a shareholder in the earnings of leading companies is and remains the most attractive investment opportunity. Gold continues to have low opportunity costs and offers security against market and currency distortions.

Zurich, end of June 2020