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Investment review - Q1 2020

6 April 2020

After a promising start, the first quarter of 2020 has undoubtedly been one of the most extraordinary and difficult periods any of us are likely to experience in our lifetimes. It goes without saying that our clients, their families, friends and all our stakeholders, and of course all those doing their best to help us get through this coronavirus crisis, remain uppermost in our minds.

We have aimed to keep you informed with our regular bulletins and updates of market events, so we will not repeat things already said here, but the end of the first quarter is a useful staging post for us to take stock of the current situation and reflect on how things have fared from an investment perspective, whilst also attempting to give some encouragement for the future.

In terms of market movements, recent falls eclipse many of those seen in the 2008 global financial crisis and we must to go back to the stockmarket crash of 1987 to see declines of a similar magnitude, particularly in the UK, where share indices have fallen by between 25% and over 30%, depending on size, with additional downward pressure coming from a market laden with oil and commodity-related stocks. Overseas market returns have been slightly cushioned by currency influences, but falls have nonetheless been very sharp and indiscriminate. Daily volatility has also been huge, not just in stockmarkets but other asset classes too as investors requiring cash have, at times, sold anything remotely liquid that they can immediately get their hands on. Thankfully, some relative calm had been restored by the quarter end, but widespread uncertainty still very much prevails as we start this next period.

All our portfolio strategies, even those with the risk budget that allows a very high commitment to stockmarkets, have generally fared better than global stockmarkets as a whole. We were not fully committed to stockmarkets for our range of strategies going into this market sell-off and have also taken steps during it to increase cash levels where we have felt there could be further difficulties ahead. Underlying active managers have also been busy taking whatever action they have felt necessary to get through this, with some taking bold decisions recently to acquire longer-term investments that were previously out of reach. We have also avoided several shorter-term hazards in less liquid investments, or those alternative investments with a more esoteric nature, where pricing can become more problematic in times of market dislocation. Having had no exposure to the commercial property market, possibly the next area to feel the full force of this crisis, has also been beneficial as funds in this sector themselves go into lockdown.

We are increasingly understanding the scale of the pandemic and its consequences as each day passes, but it is still too early to gauge its ultimate impact. Recessionary conditions are virtually assured in most areas of the world, but how deep these will be and what shape the ultimate recovery will take is, at this juncture, also very difficult to determine. The world's health professionals are working overtime to care for those impacted by the virus, as are governments and central banks – we already had huge amounts of stimulus in place before this crisis began, and now have colossal amounts more. This won't halt the pandemic, but it will help businesses and consumers through this period of crisis. But there will also be a lot of permanent damage done, much of which is still impossible to quantify.

We are still biding our time with any cash we have raised as we believe the coast is not yet clear on several fronts. UK newsflow is likely to worsen over the coming days as the virus takes a firm hold here, and a similar situation is already unfolding in the USA on a much grander scale. And then there is still the possibility that things may reappear in China and other parts of Asia now that the region is returning to work. Japan, for instance, which had to date shown good containment of the virus, is also now introducing greater social distancing and lockdown measures.

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We are, however, probably getting closer to the point where we may wish to put some risk back on the table. In all likelihood markets will move in a more positive direction well before the underlying data, and those with the sturdiest constitutions to invest at what, in due course, turn out to be the very bleakest moments of market panic are the ones most likely to be rewarded with the strongest returns from that point. Crossing the bridge from fear and uncertainty on one side to a land of optimism and opportunity on the other is often a very wobbly experience, and it can frequently take some time. We are unlikely to pinpoint the optimal time to start that journey – generally only the very lucky manage, in hindsight, to do this – but we do already have commitments to markets that will automatically benefit. We can also prepare for the next leg, which is what we are doing now. Our attention is not only likely to focus on those areas that have seen some of the sharpest falls, but also regions that are less likely to be burdened longer term by the financing of the monetary and fiscal policies currently being rolled out to address this crisis. The latter point currently points towards Asia gaining further ground relative to the rest of the world.

We are in no immediate hurry to invest the cash we have accumulated, as recent market lows could yet be re-tested, particularly as the pandemic's epicentre shifts from Europe to the USA. Furthermore, whilst it is encouraging to read that companies are conserving cash by ceasing share buybacks, cutting back on capital expenditure and suspending dividend payments, businesses and the livelihoods of millions around the globe are still being turned upside down. For those companies with strong balance sheets and durable or adaptable franchises, this should not cause too much long-term damage. But we should also be prepared for many businesses not to survive, at least in their present format or with the same scale. As this new quarter unfolds, market participants will be sifting through all the corporate numbers not only to see how much water has already flowed under the bridge, but also to assess what is coming – this is where the forward-looking statements from company management will be a key influence on markets. Close corporate engagement is an important tool that the many active managers we use have at their fingertips, and we expect them to use it to their advantage in the coming months.

All things considered, it is a relief to come through the first quarter without too much collateral damage. There is currently no expectation that current paper losses will have any permanence, but these are still understandably unnerving times for everyone: it will undoubtedly take time for markets and portfolios to show their capacity to recover and for investor confidence to return. In all likelihood this is not the first period of market uncertainty investors have had to endure along a longer-term journey, nor will it be the last: our job remains one of constructing what we believe is the optimal blend of investments that factor in the opportunities in front of us, but which also match clients' varying risk appetites and objectives. Remaining disciplined, drawing upon experience and having the ability to look through near-term uncertainty are all key components of any successful investment process, and so we would like to reassure you that we are sticking firmly to these principles and doing all we can to both safeguard your wealth and expose it to whatever opportunities we see available. To paraphrase one renowned investor, Warren Buffett, successful long-term investment is often about being greedy when others are fearful (and vice versa). There is certainly plenty of truth in this philosophy, but it does not mean acting recklessly, particularly when the investment inputs are so difficult to validate, as many are at present. This may mean we miss some of the very best opportunities, but whatever direction we do take from here we will certainly keep clients' very best longer-term interests and risk appetites at the centre of any decisions we make.

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