



WEALTH MANAGEMENT

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Good Afternoon,

Today we received an update from PortfolioMetrix regarding the Coronavirus outbreak, see below to read more.

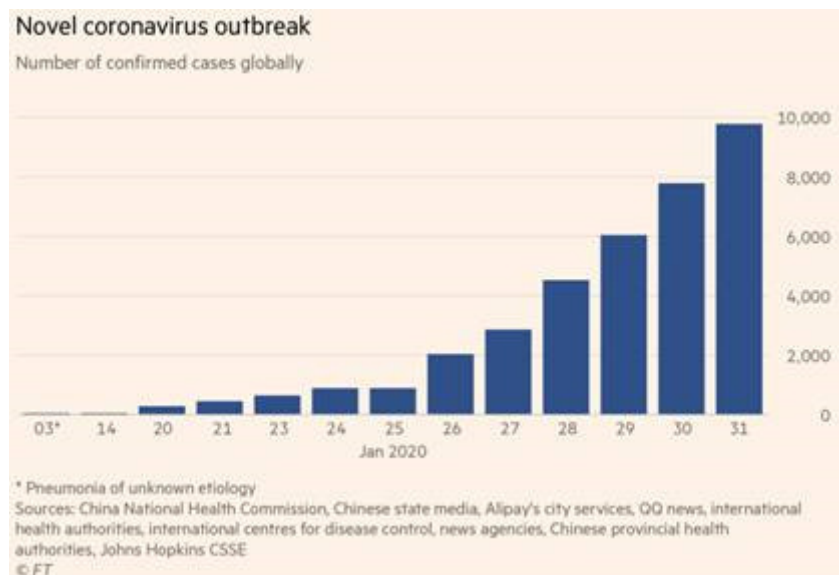
Please bear in mind that past performance is no indication of future performance as the price of funds can fall as well as rise.

If you have any further queries, please get in touch with us.

### **Coronavirus – Where do we stand today (Friday 31 January)?**

Yesterday, 30 January, the World Health Organisation (WHO) declared a public health emergency of international concern (PHEIC) over the new coronavirus epidemic. The WHO flagged the risk of the coronavirus (so called because of its spiky, crown-like appearance under a microscope) spreading to countries outside of China with weaker health systems which have less ability to deal with it.

As of this morning (31 Jan), 9,692 cases of novel coronavirus (nCoV) had been confirmed worldwide with at least 82 of those outside China, Hong Kong, Taiwan and Macau (including 2 cases in the UK). In addition, there are a further 15,238 suspected cases in China, suggesting the number of confirmed cases will continue to rise. Declaring a PHEIC is an important symbolic step which, in practical terms, makes it easier for the WHO to co-ordinate the responses of governments around the world.



Source: Financial Times, 31 January 2020

### **Should we be worried?**

We should be wary, but we shouldn't panic. So far 213 people have died from the disease, a far cry from the roughly 400,000 deaths a year caused by flu. nCov is, however, more deadly than flu, with an estimated mortality rate of 2-3% vs flu's less than 0.1%. Whilst serious, that 2-3% is lower than the roughly 10% mortality rate of Severe Acute Respiratory Syndrome or SARS (another coronavirus which killed 774 people in 2003) and Middle East Respiratory Syndrome's 34% mortality rate (a

coronavirus outbreak that erupted in 2012). It is also certainly less than the 10-20% mortality rate of the last truly serious global pandemic, the 1918 Spanish Flu which infected about 500million and killed between 50 and 100 million.

What is troubling is that nCov is obviously quite contagious, about as much as flu, with each new case infecting on average about 2.5 other people, so it's important that it is contained. This has been made more difficult in China because it emerged in the Chinese city of Wuhan at a particularly unfortunate time, just before Chinese New Year which sees a mass migration of people back to their family homes to celebrate.



Source: *Financial Times*, 31 January 2020

There are some important unanswered questions though which affect how easy it will be to contain, such as how long the virus incubates for and whether it can be passed along before symptoms show.

But there are only a few cases outside China, and, after a slow start, China itself has clamped down heavily on travel, as have other countries. Advances in medical science mean that the virus's genetic makeup could be rapidly analysed and shared with laboratories around the world. That should help with containment and development of a vaccine. Cheap face masks probably aren't that effective, but frequent hand washing (and not touching your face) is actually remarkably effective in terms of prevention (with the added advantage of helping prevent regular colds and flu, a far bigger risk to those outside China).

### How is this affecting markets?

It's difficult to completely disaggregate the causes of market moves, but fears about the virus have certainly been a large factor in the recent pullback in global equities. So far this is only a mild sell-off, but beneath the headline figures individual stock prices have moved more materially with defensive sectors (utilities, healthcare, tech, quality as a style in general) rallying, and more cyclical sectors (autos, resources, value as a style in general) as well as China-exposed travel and luxury goods retailers selling off.



Source: Financial Times, 31 January 2020 (measuring the Europe's Stoxx 600 index)

This flight to safety has also been evident in bond markets, which have rallied strongly over January as fears have risen, and yields have fallen. This also briefly led to a US yield curve inversion on Thursday 30 Jan (10-year maturity minus 3 months maturity) - yield curve inversions over an extended period have historically been a reasonable indicator of recession, so they are closely monitored.

#### How is this likely to affect markets going forward?

We don't know for certain. In previous outbreaks (such as SARS), economic damage wasn't really caused by the primary effect of the disease (people getting sick & dying) but by the secondary effects of the fear of the disease (people hunkering down and not travelling, shopping, interacting with other people, all of which affects company profits and economic growth). Given China is such a strong engine for global growth and the virus is centred there, the secondary effects are particularly worrying. SARS managed to knock 2% off China's economic growth in Q2 2003 so it's likely that the virus will have a measurable effect on global growth in 2020, although any dip is likely to be temporary, as long as the disease is contained.

As for markets, in previous outbreaks like SARS, the market sold-off sharply but then bounced back even more strongly once the outbreak started to peter out. Selling out of the market is thus risky as it risks locking in losses but not being present for the rebound.



Source: John Authers, *Points of Return*, Bloomberg

Every outbreak over the last 100 years has been contained and so has had little effect on the market, so the virus petering out remains the overwhelmingly the most likely prospect here. But it's impossible to completely rule out the incredibly serious tail risk of a global pandemic. This should definitely concern us, but careful action such as that being taken by the WHO and global governments is the correct response, rather than panic.

### Immune: world epidemics and global stock market performance



Source: Charles Schwab

**How is this affecting PortfolioMetrix portfolios?**

Coronavirus is a classic 'black swan' – an unexpected but high impact event. But the PortfolioMetrix portfolios are diversified precisely because although we don't know about specific black swans in advance (or when they'll occur) we have always believed that it's best to prepare for them in advance by building robust portfolios, rather than trying to react after the fact. Indeed, our rebalance in December, which amongst other objectives aimed to further diversify portfolios by adding in listed infrastructure and trimming emerging markets, has proved helpful month to date. Recently added M&G listed infrastructure (in Core Active portfolios) is currently up 4.15% over the month in sterling terms (as of the morning of 31 January).

In addition, where mandates permit, we also select active managers who can react quickly to new information as it emerges which helps keep client portfolios nimble.

As of the morning of 31 Jan, most portfolios are currently slightly up month to date, albeit our riskiest portfolios are very slightly negative.

It is likely, however, that portfolios will be volatile for the next few weeks as we learn more about how serious this strain of coronavirus actually is. We are not planning any knee-jerk reactions (which risk missing out on a rebound) but we are monitoring the situation closely.