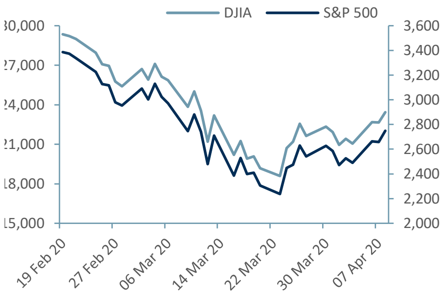
SPOTLIGHT

UPDATE

Friday, 10 April 2020

DJIA/S&P↓>30%



DJIA vs. S&P 500 (dark line))

WTI↓>113%

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ACF EQUITY RESEARCH

COVID - 19

Global Markets Future Developments

Global capital markets will recover much of their losses far quicker than anticipated by many, and ahead of any economic revival. On the 10th of March 2020 we began briefing corporates on the impact of COVID-19 on capital markets. In this update we extend the data to support our original analysis, which you can find in this note. COVID-19's effect on the global stock markets was unexpected and unforeseen causing a market reaction that had not been experienced since the 2008 financial crisis. However, history shows us that market volatility is just a part of market behaviour. All markets exhibit a 'boom and bust' trend as part of their stock market lifecycle. With government intervention and the introduction of fiscal stimuli, we can already see an uptick in the markets over the past couple of weeks. What we have seen over the years since the great depression is that the actual time it takes for markets to recover to a new all-time high has been contracting.

- With global stocks falling more than 20% since the start of the COVID-19 pandemic, we have entered a bear market;
- Aggressive government intervention, monetary and fiscal, will help the capital markets bounce back;
- Chinese growth rates of new cases have flat lined after the first 5 weeks of exponential growth;
- WTI Crude oil prices have fallen to their lowest since 2002, currently at $22.76/bbl.

COVID-19

COVID 19 has had an unprecedented effect on global stock markets, not seen since the 2008 financial crisis, but its effect on markets will be short in duration.

By Friday 20 March 2020 the world entered a bear market with major indices recording decreases of over 30%.

We have entered a bear market with stocks falling more than 20% since the start of this pandemic. The most notable summary of these stock falls is the US Dow Jones index (representing the US's largest industrial companies), which by Friday 20th March 2020 had recorded a 35% drop since 19 February 2020 (when Italy's COVID outbreak became market news). Over the same period the US's S&P 500 was down 32%, the US technology index the NASDAQ was down 30% and the UK's FTSE 100 had lost 30% of its value.

Aggressive government intervention, monetary and fiscal, will be essential in helping the markets bounce back.

However, **this is not the first time** that markets have been hit this dramatically and **nor will it be the last**. With aggressive government intervention (i.e. both fiscal and monetary policy, and which we have seen over the last two weeks) capital markets always bounce back. That is the nature of stock markets. They overshoot and undershoot their responses to dramatic, indeed any, news.

Below we have illustrated the progression of China's COVID-19 pandemic in conjunction with the declines in US and UK major indices. Since the beginning of its COVID-19 outbreak in conjunction with stock market effects in the current crisis and the behaviour of stock markets after the 2008 Financial Crisis and the Great Depression.

Growth rates of cases in China are flat lining with rates of almost 0%.

Based on the recent statistics, the rate of outbreaks in China continues to decrease. Factories outside Wuhan province (the epicentre of the Chinese COVID-19 outbreak) are already coming back on stream and heading towards full capacity, based on our research. When looking at the actual growth rates of outbreaks we can see that in China they have decreased significantly as of 14 Feb 2020 growing by only 6% compared to 25% growth rates prior to this date, and the change was dramatic. See Exhibit 1: below, which shows cases continue to increase but at a minimal rate of almost 0%. Therefore, even though the number of cases peaked within 4-5 weeks after growth became exponential, they stabilised within 2 weeks after the peak.

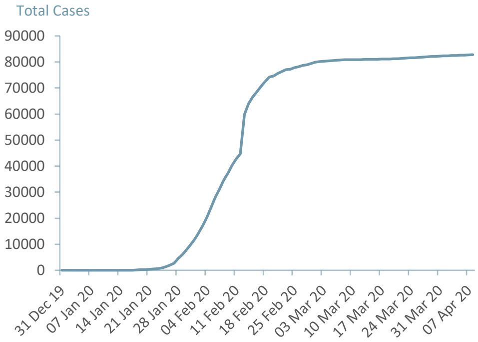
Rather than years, the trends and data suggest recovery of financial markets will take months and not years.

We are already coming towards the last part of the current period of extreme market volatility. We believe the data suggests that financial markets will recover very fast after Europe, UK and the US leave the exponential growth phase of the pandemic. **Rather than years, the trends and data suggest recovery in financial markets is likely to take months.**

Exhibit 1: **China infection rates (flatten to zero after 5 weeks)**

The Chinese growth rate in new cases of COVID-19 flattened out after just 5 weeks after entering the exponential growth phase.

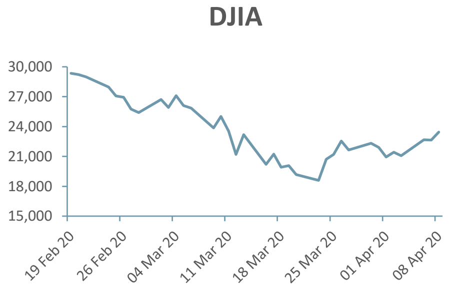
Global stock markets began their crash once the pandemic hit Italy around 19 February, the point at which the Chinese infection rate began to flatten. This suggests that Italy is 3 to 5 weeks behind the peak infection rate at which point infection rate falls off dramatically.

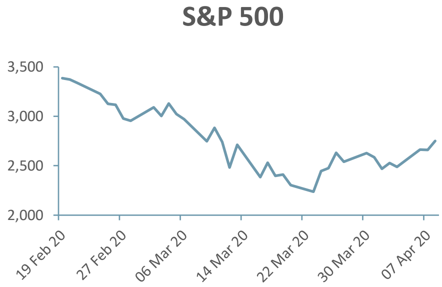


2020 COVID crash – US's DJIA

2020 COVID crash – US's S&P 500

Global markets begin to dive 19th Feb just after Italy announces major infection incident. At the same point Chinese infection rates growth flattens to nearly zero. Our research suggests Chinese factories are already returning to full capacity outside of Wuhan province.

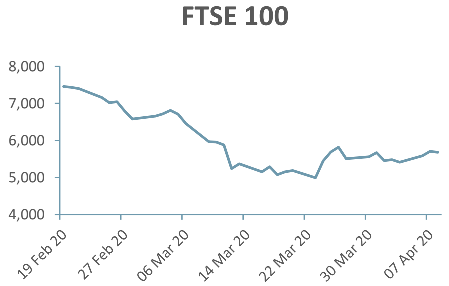


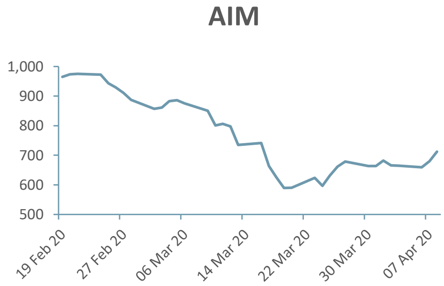


2020 COVID crash – UK's FTSE 100

2020 COVID crash – UK's AIM

The global wave of fiscal stimuli is already showing signs of an uptick in the markets over the last couple of weeks.





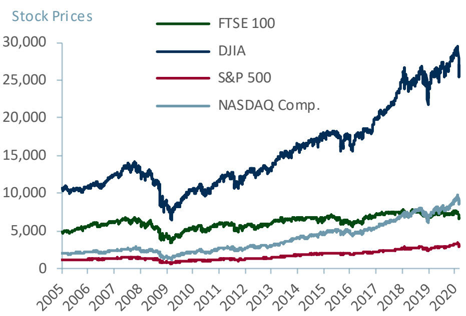
2008 Financial crash

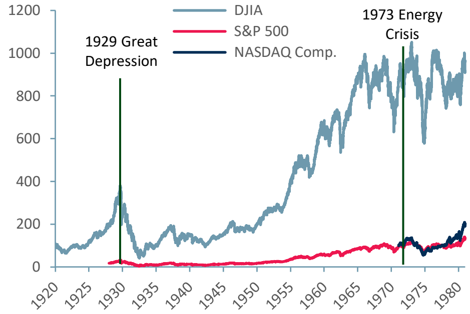
1929 Great Depression

How long will markets take to regain the majority of their losses after the COVID-19 crash? We think it will be months rather than years.

5 years – financial markets recovery period post the 2008 Financial crash.

20 years – financial markets recovery period post the 1929 Great Depression crash





The current market crash is consumer led and recovery is likely to occur rapidly.

The resilience in markets is further illustrated by the 2008 global financial crisis. Even though the crisis began on 15 September 2008 with the fall of Lehman Brothers, leading to very significant market crashes around the world, US markets started regaining positive momentum towards the end of 2009 and the FTSE 100 rebuilt all its losses by mid-2010. The Financial Crash of 2008 was complex and difficult to solve as it threatened the entire global capital markets system. The current crash is consumer lead and the majority of the recovery is likely to occur very rapidly when it starts due to the enormous effort by governments to stimulate growth and to support and re-build confidence in the economy and so the confidence and positivity of capital markets.

The US markets 'boom and bust' trend is a part of the stock market life cycle.

Over time, following the great depression, US markets have shown us that the 'boom and bust' trend is part of the stock market lifecycle as is highlighted in Figure 7. On 'Black Monday' 28 Oct. 1929 the Dow Jones experienced a decline of 12.8% and on 'Black Tuesday' a further decline of 12%. It took about 20 years for the market to recover from Black Tuesday however, we saw that during the 2008 financial crisis it only took the FTSE 5 years to recover.

Volatility in markets is a given. It is part of their nature. However, as we have observed the time it takes to 'bounce back' from major catastrophic events from a capital markets perspective or to revive the markets diminishes significantly after each crisis.

The speed and breadth at which global communication is growing is increasing the recovery rates of markets

This increase in the rate of recovery of global markets is in large part, in our view, due to global communications developments and the speed at which data is now processed and shared – crashes happen quicker and go deeper but the recovery period is also becoming quicker. We see the same trends in the business cycle, and largely for the same reasons, the cycle gets shorter and shorter and this appears linked to the greater and greater speed, depth, and breadth of global communications.

Our team has worked through four global market crashes or corrections of depth and significance. The market will recover and the majority of the recovery will come early and quickly.

Fiscal stimulus will increase disposable income and in turn feed into businesses.

We are of the view that **the economic recovery will be driven by the global wave of fiscal stimulus** we are watching build at the moment, occurring in both developed and developing countries. Any **fiscal stimulus will increase disposable income** for consumers, which feeds directly into businesses. This in turn will stimulate the rest of the economy and **historically such changes of outlook hav**e **been recognised by wholesale market participants before it has been recognised by other of investors.**

Glossary

AIM	AIM is a sub-market of the London Stock Exchange and was launched on 19 June 1995.
BBL	bbl is the abbreviation for 'barrel of oil'. In the US and Canada, a barrel of oil is 42 US gallons or 159 litres.
COVID-19	Corona Virus Disease 2019 is the deadly disease that has caused more than 1m cases and 100,000 deaths world-wide.
DJIA	Dow Jones Industrial Average index tracks the stock performance of 30 large companies listed on US stock exchanges.
FTSE 100	Financial Times Stock Exchange 100 index tracks the stock performance of 100 companies, with the highest market capitalisation, listed on the London Stock Exchange.
NASDAQ Comp.	NASDAQ Composite index is comprised of common stocks and similar securities listed on the NASDAQ stock market.
S&P 500	Standard & Poor's index tracks the stock performance of 500 large companies listed on US stock exchanges.

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