Market Observations - 26 March 2020

TOREVELL
&PARTNERS
WEALTH MANAGEMENT
5 Oxford Court
Manchester M2 3WQ

Over the last few days we have spoken to a number of fund managers to get their views on the events of the last few weeks. Some of the key observations are summarised below.

- The scale of recent market falls is not unprecedented, but the speed of the decline is. The S&P500 took only 16 trading days to fall 20%. During the Great Depression of 1929 it took 30 days to fall 20% and in the Great Financial Crisis it took 188 trading days to fall this far.

  The S&P500 has fallen 30% on 8 previous occasions. It has taken the S&P500 only 22 trading days to fall 30% this year. The next closest in terms of time was in the Great Depression when it took 31 trading days.

- No areas of the market have been immune to losses over the period; this includes credit and government bonds. To compound matters, as investors searched for liquidity they also sold gold, which fell 12.5% intra-month, before rallying again. The speed and scale of the market movements, on the upside as well as the downside is unprecedented. Two of the best 11 days ever in the S&P 500 have occurred this month when the market was up over 9% each day.

- The distress in the high yield credit market is still unfolding. Yields of the lowest rated bonds are trading above 10%. The obvious areas of distress are in energy in which prices were down 50%.

- There has been a huge monetary and fiscal stimulus response by central banks and governments around the world equating to 9% of the world's GDP. The scale and speed of response is again faster than on any previous occasion.

- All our fund managers focus on the balance sheet of their companies. They have redoubled their efforts, stress testing the balance sheets of the companies they hold to ensure they can withstand a prolonged period of cash flow deterioration.

- They are talking to the management of the companies, about how they are managing their cash flow for this period, what covenants they have on their financing and who they owe money too. They know this information already, but are ensuring they have the most up to date information given that this is a fast changing environment.

- Equity market falls have been quite indiscriminate with utility companies falling alongside cyclicals. There are some obvious sectors that have been hurt more than most, but markets are seemingly not paying much attention to valuation and balance sheet strength. They will eventually and that is when our managers will outperform.

- Those with higher than normal cash balances have been buying selectively in the market as opportunities present themselves. No one knows whether the bottom of the market is in yet. However the potential in the market place for significant rallies like we have seen over the last week is large. The market is capricious.

Directors
A Torevell Bsc (Econ)
M P Torevell MA (Cantab), ACA
E C Holden BA (Hons), MA
A J Valentine MA (Oxon), ACA
P A Lee DL, MA, LLM

Contact details
T: 0161 281 6400
T: 0161 883 3894 (recorded line)
F: 0161 281 6500
E: enquiries@torevellpartners.co.uk
W: www.torevellpartners.co.uk

- Valuation focussed managers have commentated that their opportunity set had become a lot bigger in recent weeks. Companies whose long term prospects remain positive and whose balance sheets are sound, will recovery quicker than most.

- The rally in the market of the last few days, in the face of deteriorating Covid-19 data and unprecedented weakening in the real economy is normal in bear markets. It has been helped by the pension rebalancing that is taking place a quarter end. Goldman Sachs estimates that the rebalance is to buy $214 billion equities and sell the equivalent fixed income. The next largest total was at the end of 2018 when there was a $82 billion of rebalance.

- Managers expect that Q2 and Q3 earnings to be poor. Company dividends are going to be tested, but the extent is difficult to gauge. Many companies have already halted their stock buyback programs and some have given guidance on dividends, but it is really too early to tell. We are in constant conversation with our fund managers and others through this period and will report when we have clear information.

- In the 2008 Great Financial Crisis the market bottomed 3 months before the economic data got better. When the rally does come, given the amount of stimulus in the market and the amount of selling that has occurred already, you will miss the best returns if you are out of the market.

- Patience is the key.