Current Focus

February 2020

A monthly market comment from Rivers Capital Management. Views expressed here are subject to change and for professional advisors only

INTELLIGENT INTUITIVE INVESTING

Market Comment

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Summary

- The Coronavirus stopped what was a strong start to 2020 for investors
- This flu-like illness has spread quickly and caused disruption across the region
- The illness has effectively paused economic growth in China for the first quarter
- The impact on global trade will be high unless the illness is successfully contained
- Enhancer valuations remain high and we maintain a defensive tactical allocation

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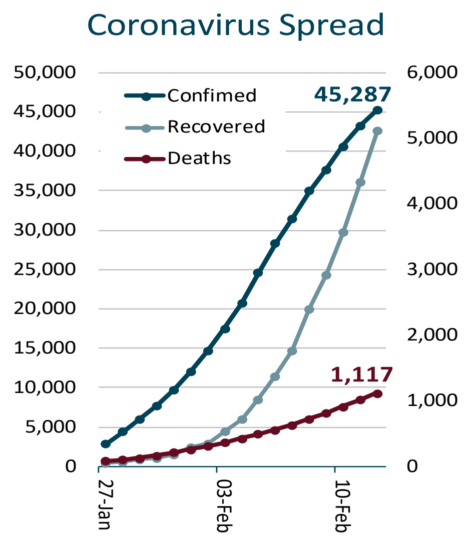
2020 started with a much more optimistic investment outlook from investors than 2019 did. Progress in the US-China trade negotiations, more certainty over Brexit and a significant Conservative party majority in Parliament contributed to a confident start to the year for markets. Many , including us, were still concerned over extended valuations and geopolitical tensions but it did feel like the economic slowdown, that was threatened from early last year, had been averted, or at least materially delayed. Whatever these concerns, no one predicted the rise of the Coronavirus from within China. This initially untreatable strain of influenza has quickly become a global concern despite still being primarily contained within mainland China. The initial market reaction to rapidly escalating infection numbers wiped out the market gains of the first few weeks of the year, but those losses have, so far, not been sustained. This month we look at the possible impact of the virus and why it adds to what we expect to be a volatile period for investors.

While comparisons can be drawn between the Coronavirus and the SARS epidemic of 2002/2003, any economic impact assessment between the two should be made with care. SARS had a higher mortality rate and infected people more quickly, but the global importance of today's Chinese economy compared to its influence in 2003 makes the Coronavirus a potentially far more significant risk. China's share of global GDP, trade, and demand for most commodities has more than doubled since 2003. China's economy is also far more levered today, and in 2003 the global economy was coming out of an economic downturn rather than 10 years since the last one, with valuations high. A sharp drop in Chinese demand will be more damaging to global growth in the near term than it was in 2003. On the flip side China now has much more fiscal and monetary firepower and the response to the deflationary impact of the virus, including the hit to business and consumer sentiment, is likely to be large. So far commodity prices, especially oil and base metals, local emerging market bond yields and regional currencies have fallen, but the initial global equity index losses have already been reversed. In early February the effect appears to be modest but the risk of a further escalation of infections and impact from this virus remains high.



Source: www.coronatracker.com

Coronavirus began in Wuhan, a city of more than 11 million people and the capital of the Hubei province in China. Statistics, for what they are worth, show that the total number of deaths from the virus exceeded 1,000 by February 10th. The death toll was all in mainland China except for one person in Hong Kong and another in the Philippines. The number of confirmed cases around the world has risen to more than 42,000 although it is not known how many more people could be infected without having had the diagnosis confirmed. Many reports show the spread of the illness is slowing but there are so many variables it is difficult to draw accurate conclusions. There is little doubt that measures to contain the virus will weigh heavily on growth at the start of the year, but beyond that, much will depend on how it spreads. The extensive efforts to contain the virus have caused economic growth in China to slow abruptly. The longer they remain in place, the more they will hit demand elsewhere in the world too. Emerging Asia is most vulnerable to any virus-related disturbance to manufacturing supply chains.

Industry-level data suggest that temporary disruption should have little macroeconomic impact on developed markets although some manufacturers, especially the Euro automakers, are reliant on components that come from China and have already delayed orders. Even in the US the auto sector has relatively large supply chain links with China, with some, including Tesla suggesting they are just weeks away from shutting plants due to a dwindling supply of parts. The effects are highly uncertain, and at the very least there could be serious consequences for individual firms, which could hit asset prices, especially in the tech and autos sectors.

Even if the Coronavirus outbreak in China is brought under control, Capital Economics estimate that the economic disruption related to the virus will cost the world economy over $280bn in the first quarter of this year. That is significant, but it is notable that they do go on to say that, if the virus is contained sooner, the lost output will be made up in subsequent quarters and that world GDP will reach the level it would have done had there been no outbreak by the middle of 2021.

What is certain is that the Coronavirus outbreak has made the near-term economic outlook uncertain. That uncertainty seems not to be reflected in what are undoubtedly high market valuations as confidence from investors remains positive. Even if the Coronavirus can be overlooked, which would make the global economic outlook for 2020 appear balanced, Enhancer assets appear to offer little value. We continue to believe that Enhancer assets will be subject to a correction, which will allow some realignment, before further advances, but provided the virus doesn't become a global pandemic, we do not expect a change to the positive trend. Easier financial conditions, receding trade tensions, a pickup in global manufacturing, and whatever reflationary policy that is expected from China, should underwrite sustained economic global growth in 2020 but current valuations remain on the high side.

Market Returns (£) - 31st Jan 2020	1 Month	3 Month	YTD	1 Year	3 Year	S/I*
Anchors						
Cash + 1%	0.2%	0.5%	0.2%	1.8%	5.0%	5.9%
Inflation Linked UK Bonds	2.7%	0.1%	2.7%	7.9%	8.5%	13.9%
Gilts	3.8%	1.4%	3.8%	10.1%	16.2%	12.7%
Global Government Bonds (hedged)	1.9%	0.9%	1.9%	6.8%	10.8%	6.6%
Enhancers						
Global Corporate Bonds (hedged)	2.0%	2.2%	2.0%	10.9%	14.8%	14.0%
Global High Yield (hedged)	0.3%	2.6%	0.3%	7.1%	12.5%	20.9%
Emerging Market Bonds (hedged)	-0.8%	-1.0%	-0.8%	6.0%	13.0%	20.0%
FTSE 350 TR Index	-3.3%	2.0%	-3.3%	10.6%	18.2%	31.7%
FTSE UK All-Small Cap	-0.7%	8.6%	-0.7%	12.6%	23.9%	47.0%
Global Equity (MSCI)	-0.1%	3.3%	-0.1%	19.7%	34.6%	53.6%
European Equity (MSCI)	-2.1%	0.9%	-2.1%	14.6%	22.4%	37.9%
US Equity (S&P)	0.4%	4.6%	0.4%	20.7%	40.9%	63.9%
Japan Equity (Topix)	-2.0%	-1.5%	-2.0%	9.8%	16.8%	39.5%
Pacific Ex Japan Equity (MSCI)	-4.4%	0.5%	-4.4%	6.0%	24.6%	44.4%
Emerging Market Equity (MSCI)	-4.2%	0.4%	-4.2%	5.3%	21.7%	40.3%
Chinese Equity (Hang Sang)	-5.9%	-3.0%	-5.9%	-1.6%	19.5%	44.5%
Indian Equity (Nifty)	-0.3%	-1.7%	-0.3%	10.2%	27.4%	35.7%
Diversifiers						
Commodity Index	-6.9%	-6.9%	-6.9%	-5.6%	-14.2%	-9.9%
Gold	4.5%	2.4%	4.5%	18.8%	22.3%	18.2%
Silver	1.1%	-2.6%	1.1%	10.3%	-5.3%	-6.2%
Brent Oil	-11.8%	-5.1%	-11.8%	-5.3%	0.5%	19.0%
UK Property	0.1%	0.7%	0.1%	1.2%	12.7%	14.2%
Global Property Shares	-2.8%	4.2%	-2.8%	16.8%	30.1%	31.4%
Rivers Model Portfolios						
Rivers Preservation Portfolio	*1.4%*	*1.6%*	*1.4%*	*5.2%*	*8.3%*	14.1%
Rivers Cautious Portfolio	*1.3%*	*2.2%*	*1.3%*	*8.5%*	*14.2%*	24.4%
Rivers Balanced Portfolio	*0.9%*	*2.5%*	*0.9%*	*9.9%*	*18.2%*	31.1%
Rivers Adventurous Portfolio	*0.8%*	*2.6%*	*0.8%*	*10.4%*	*18.9%*	33.8%
Rivers Aggressive Portfolio	*0.5%*	*3.6%*	*0.5%*	*12.3%*	*22.6%*	40.8%
Rivers Cautious Income Portfolio	*-0.1%*	*1.2%*	*-0.1%*	*7.0%*	*10.0%*	15.0%
Rivers Balanced Income Portfolio	*-0.5%*	*1.3%*	*-0.5%*	*7.8%*	*12.7%*	21.9%

Source: Financial Express in GBP (unhedged unless stated) as at 31st January 2020. *Rivers Portfolios since launch June 30th 2016

Model Performance is indicative only and is net of Rivers Capital Management Charge and Underlying Fund charge but not advisor or platform costs.