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# Multi-Asset: Coronavirus update

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Multi-Asset | March 2020

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We came into the turn of the year with a view that the global industrial cycle was turning after an industrial recession that came with a mild global profits recession.

Equity market performance appeared to be driven by bond market-related re-rating as government bonds discounted supportive monetary policy and credit markets discounted a slow growth environment. A lot has changed – and it has changed with unanticipated speed.

Over the past month we've seen developed equity markets lose up to 32%. Our Dynamic Real Return strategy is down 8.8% year-to-date (as at 12 March 2020). This is more participation in the downturn than we would have liked, but not miles off the aim of 5% down in a 20% equity down year and 12% up in a 20% equity up year.

Putting this in a slightly longer context, the strategy is now down over a year, after the sell-off ending on 12 March 2020. Given most developed market equity markets are down 10%-20% over the same period this is a defensible outcome.

Things that worked during the past three months:

- Choosing to increase portfolio risk through a variety of forms of risk exposure rather than merely equity risk (ie, emerging market local, short-dated high yield)
- Choosing to have a lower GBP exposure in the portfolio immediately following the election
- Choice of Asian equity within regions, with China, Taiwan and Korea outperforming in a weak market.
- Reducing duration in 2040 TIPS at around 0%.

Things that have been poor so far:

- Restoring some of our equity exposure to the portfolio after the first 10% drop in index values
- Additions to UK equity – which has underperformed

### The context for our actions so far

The speed of the equity market moves have been astonishing. We have often come in with fresh news overnight (mass school closures, travel bans, geographic lockdowns) to find indices down 4%-8%.

Portfolio activity is based on an overarching understanding that Covid-19 is a serious – but transitory – threat to human life and the global economy. The economic disruption that the virus, and public health responses to the virus, bring will be short lived if they are well handled from a public policy perspective.

### What do we plan to do?

We have not been immune from the sell-off, but we have plenty of dry powder in the portfolio. Portfolio risk is not high and as a team we continue to think that extending risk across a range of preferred risk assets as spreads rise is the right approach. Though as we speak, we have been adding to risk through specific regional equities today, albeit in a measured way.

### Why haven't we been buying duration-bearing government bonds?

Long-dated core government bonds have performed well this year as markets have sought safe havens amid discounted central banks moving to and staying at their lower policy bounds. The self-professed lower policy bounds of core central banks can change, but are around 0.1% in the UK and US, -0.5% in Europe and -0.25% in Japan. If 10-year government bonds move quickly to this lower bound from here (pricing in staying at the lower bound for the next 10 years) the prospective returns from government bonds are modest, but positive (apart from in Germany).

If we had a view that central banks would shift to their lower bound, and that bond markets would then price them to stay there for the next 10 years, we would see the value of building government bond positions from here. But our understanding – and portfolio activity – is based on an overarching understanding that Covid-19 is a serious but transitory threat to human life and the global economy. As such, portfolio activity regarding government bond duration has been to cut into the rally rather than build.



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