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MONTHLY NEWSLETTER

March 2020

KEY ECONOMIC DATA PUBLISHED IN FEBRUARY

- China's Caixin PMI Manufacturing collapsed in February to 40.3, versus market expectations of 46.
- China's Caixin PMI Services index also plunged in February to 26.5 compared to 51.1 the previous month.
- Economic sentiment in the Euro-zone dropped in February (ZEW survey at + 10.4 vs. + 25.6 in January). The PMI Composite number was higher at 51.6 (51 expected).
- In Germany, economic sentiment (ZEW survey) dropped in February (+ 8.7 vs. + 26.7 in January). The IFO Business Climate Index was stable at 96.1, above expectations of 95.3.
- US consumer confidence was 130.7 in February, below forecasts of 132.
- The Markit US Manufacturing PMI Index declined in February to 50.7, less than forecasts. The Services PMI was also lower at 49.4, below market expectations of 53.3.
- US payrolls in the private sector rose by 206K in January vs. forecasts of + 155K, with December numbers revised from 139K to 142K.

THE FEDERAL RESERVE MAKES A 0.5% EMERGENCY RATE CUT TO A TARGET RANGE OF 1% - 1.25%

0.80%

THE 10-YEAR U.S. TREASURY YIELD AT AN ALL-TIME LOW IN EARLY MARCH

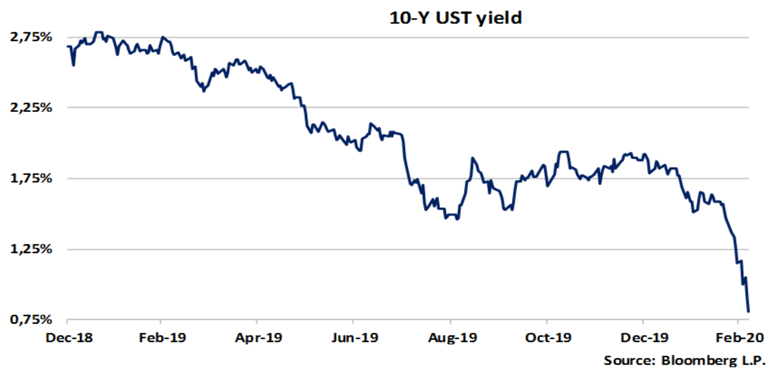
INVESTMENT PERSPECTIVE

If January was an eventful month, February proved to be much more dramatic as virus fears gripped the markets. Equities ended the month in freefall and the slide of bond yields accelerated. During the last week of the month, the 10-year Treasury yield dropped by a whopping 32bps to fast close in on the psychological level of 1%, whereas the major equity indices fell by around 12%, their worst weekly drop observed since the great financial crisis in 2008. The MSCI World Index, in local currencies, posted an 8.2% monthly loss. The 10-year Treasury and Bund yields fell by 36bps and 17bps respectively to end-February levels of 1.15% and - 0.61%. In the commodity space, oil prices dropped into bear market territory while technical factors prevented the price of gold from benefiting from the lower real yields and from a weaker dollar.

The end-February plunge of equity markets was extremely violent as it was the fastest US stock market correction in history; the S&P 500 dropped by 12.8% in just seven days of trading, wiping out over five months of gains, with the Dow Jones Index closing down by more than 1’000 points twice in a week. As was the case in December 2018, markets were totally driven by sentiment and a self-fulfilling negative spiral relentlessly drove prices lower. The dollar was another asset that was badly impacted by the end-of-month events. The collapse of Treasury yields and high Fed rate cut expectations were the main drivers for the sudden depreciation of the dollar as it rapidly lost more than 2% against the euro, from 1.079 dollars per euro on February 20 to 1.103.

The impact of the coronavirus on economic data is only starting to produce its effects; Chinese official and Caixin PMI Manufacturing numbers for February have plunged to levels well below those observed during the financial crisis. Upcoming data worldwide will increasingly reflect the contraction of business activity, reduced travel and supply chain disruption.

THE 10-YEAR US TREASURY YIELD PLUNGES TO AN ALL-TIME LOW



The year-to-date trend of US Treasuries has confounded consensus forecasts, once again. The chart shows that 10-year yields have just dropped to 0.8%, an all-time low. The quick rise of market expectations for Federal Reserve rate cuts and the sustained demand for safe haven assets have been the main drivers of the prevailing trend. At the time of writing, the Fed has just taken a rare emergency decision to cut its rates by 0.5%, the first time it has acted before a planned meeting since the financial crisis in 2008.

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INVESTMENT STRATEGY

The outbreak of the COVID-19 virus represents a totally unexpected and unforeseeable event, otherwise known in capital markets as a black swan event. We are not qualified to be able to predict the final outcome of the virus outbreak but things are likely to get worse before they get any better. Following the violent end-of-February correction of equity markets, the first week of March looks more like a roller-coaster with huge swings in both directions; it is likely that it will take some time for markets to stabilize.

In view of this extreme level of uncertainty, we have decided not to cut our equity allocation but to buy some protection. This tactical decision allows us to maintain our equity exposure which is based on our long-term outlook. It also contributes to mitigate portfolio losses were the ultimate impact of the virus outbreak prove to be much more damaging to the economy and to financial markets. Were markets prove to be resilient, the purchase of this protection will represent an opportunity cost for the portfolios, a limited price to pay in view of the potential drawdown of equity markets in a worst-case scenario.

PORTFOLIO ACTIVITY/NEWS

Following a strong rebound of risky assets during the first half of February, the remainder of the month proved to be much more hurtful to the performance of the portfolios. Only a small number of positions produced positive contributions; it was nevertheless reassuring to observe that some hedge funds ended with monthly gains. All equity funds ended in negative territory, unsurprisingly. Japanese equities were the worst detractors while emerging markets' ones fared better in relative terms; we still believe that the valuations and the upside potential of both asset classes will be supportive when markets eventually regain their composure. The drop of most credit funds was contained in view of the widening of credit spreads, especially as a result of lower risk-free rates.

At the very beginning of March, we took advantage of a strong bounce of US equity markets to strengthen the portfolios by purchasing an end of June S&P 500 Put. The impossibility to predict the ultimate impact of the spreading of the COVID-19 virus on economic activity and on corporate earnings in the upcoming months led us to buy protection.

MARKETS ARE HAVING TO FACE AN INCREASING LEVEL OF UNCERTAINTY

	End 2019	January 2020	February 2020	Month	2020
Equities					
S&P 500	3230.8	3225.5	2954.2	- 8.4%	- 9.1%
Euro Stoxx 50	3745.2	3640.9	3329.5	- 8.6%	- 11.1%
MSCI EM	1114.7	1062.3	1005.5	- 5.3%	- 9.8%
Yields					
UST 10-year	1.92%	1.51%	1.15%	- 36bps	- 77bps
Bund 10-year	- 0.19%	- 0.44%	- 0.61%	- 17bps	- 42bps
BBB EU	0.97%	0.65%	0.70%	+ 5bps	- 27bps
Currencies					
EUR/USD	1.121	1.109	1.103	- 0.5%	- 1.6%
USD/CHF	0.967	0.963	0.965	+ 0.2%	- 0.2%
EUR/CHF	1.086	1.069	1.065	- 0.4%	- 1.9%
GBP/USD	1.326	1.321	1.282	- 3.0%	- 3.3%
Commodities					
CRB Index	185.8	170.3	159.4	- 6.4%	- 14.2%
Oil (WTI)	USD 61.1	USD 51.6	USD 44.8	- 13.2%	- 26.7%
Gold	USD 1517	USD 1589	USD 1586	- 0.2%	+ 4.5%