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Asset Managers Have Clashing Views On Coronavirus Severity: Webinar

The duration and severity of coronavirus is still up for debate as investors look to gain an understanding of its economic impact.

Those differing views were on display during a webinar hosted by marketing and distribution firm **Sondhelm Partners** on Friday.

The current market instability is likely to persist for around 18-24 months, **Securian Asset Management** Senior V.P. **Craig Stapleton** warned, noting that the outbreak has exposed deeper weaknesses in the economy.

“One of the perverse things that I was worried about going into this is that there aren’t any true market makers anymore,” Stapleton said. “Banks don’t have balance sheets to take risks. Hedge funds aren’t stepping to the plate. They don’t have the leverage or the ability to take big risks and there’s no natural buyer of risk.”

The lack of strong market makers to assume risky securities has exacerbated the problem of volatility, Stapleton argued.

“We’ve seen days of moves on the [**Standard & Poor’s**] 500 that have been plus or minus 10% plus, which we haven’t seen since 1987,” he said. “I do believe that that’s just a correlation to the deficit in market-making ability and the lack of liquidity, the lack of risk takers.”

Management of equity risk has become a more important question than ever, Stapleton observed. So long as interest rates remain low, fixed-income will yield dismal returns, and so calculated risk taking in the equity markets will be critical for investors balancing their portfolios. Even though he expected the economic downturn from COVID-19 to be relatively short-lived, Stapleton continues to believe that the question of risk management will remain relevant for a long time to come.

The responses of world governments to the current pandemic may also carry long-term economic consequences, suggested **Clive Gillmore**, ceo and cio of **Mondrian Investment Partners**. He noted that coronavirus began as an earnings event, but has mutated into a capital event as the virus spread from China to the rest of the world.

Earnings events pose little threat to an investment portfolio, but a capital event can result in significant long-term damage, and the unprecedented lockdown measures adopted to contain the disease also threaten the revenue of entire industries. This revenue event could prove especially devastating to firms with high operational leverage, where even minor declines in monthly revenue leave a company unable to meet its current obligations, he said.

“Never before in my career, which dates back to the early 80s, has there been a situation where revenue has trended to zero, if only on a short-term basis, in a range of industries,” Gillmore said. “The combination of income event, certainly, revenue event, certainly, capital event, probably, operational leverage, definitely, financial leverage, probably, is a problem for an equity investor.”

The severity of the short-term prognosis necessitates government action, but once governments move to stabilize the economy, Gillmore feared that the genie of elevated taxes, more stringent business regulations and an enlarged welfare state may not return to the bottle.

“Banks are used to being regulated. What happens if companies need to be regulated as a going concern? Instructions on capital positions, liquidity positions and dividends? That is not an impossibility,” he warned.

Gillmore views the current environment as difficult but not impossible to navigate for investors, noting that international markets currently enjoy reasonable amounts of liquidity, although the flight to safety has damaged currencies besides the dollar. However, Gillmore also pointed out that 2019 saw the lowest global growth figures since the 2008 financial crisis and concluded that the economy was nearing the end of the business cycle even before the current pandemic.

JAG Capital Management CEO and CIO **Norm Conley** struck a more optimistic note, positing that the severity of the current crisis is driven by short-term concerns and may be mere months or even weeks away from reversing itself.

“What we’ve got is a self-imposed, biologically-driven crisis, that has, in a uniform way globally, caused policymakers to shut down, put into hibernation, the vast majority of GDP around the world,” Conley said. “One thing we know for sure is that that is going to be a temporary phenomenon… We’re probably looking on the order of weeks here in the U.S. I don’t know if President [**Donald**] **Trump**’s target of April 12 is going to hold or not, but we’re talking weeks, probably not months here in the U.S., and there may be a little bit of an extension in other areas of the world.”

Given this outlook, Conley expressed concern that central banks and governments may be overreacting with the levels of economic stimulus currently being considered. But he also saw opportunity in the current environment for forward-thinking investors.

“We continue to like some of the very high-quality, very strong balance sheet, very strong free cash flow technology companies like Microsoft and Adobe,” he said. “This is probably more controversial, we also like semiconductor stocks. Some of these companies are going to come out of this with some pent-up demand.”

Conley also saw reason for hope in the credit markets, where 10-year Treasury spreads peaked on March 23 and have subsequently declined. He noted that the S&P tends to recover in the weeks and months following a peak in Treasury spreads and, because of this, feels that now is the time to begin considering the opportunities to be found in a post-COVID-19 market.

A recording of the webinar can be accessed here.