KEHRLI & ZEHNDER

INVESTMENT COMMENT

March/April 2020

- **COVID-19**

  After reacting late, the European and U.S. governments have taken decisive action to reduce the spread of the virus. Switzerland is almost on lockdown. Each of our lives, plans and activities have been turned upside down in unexpected ways, requiring utmost flexibility and resilience in a challenge that we are facing as a society. But it is the right thing to do. As several Asian countries have demonstrated, the virus can be contained and the crisis deflated if we all exercise self-restraint.

- **Monetary plus fiscal stimulus**

  Central banks around the world are injecting liquidity into the financial system. Volatility has increased to levels last reached during the financial crisis in 2008. The Fed lowered rates to zero and announced a widespread QE program, so did the ECB. Another strong signal was the recent announcement by the US government to invoke the Defense Production Act that gives the president vast powers to shift domestic production to products of national (health) security.

  The SNB announced that it will grant banks a larger exemption from negative interest rates allowing them to be more lenient with their clients. It also intervened in the FX market. The goal of this concerted effort by the SNB and the Federal Council is to help the backbone of the Swiss economy - small and midsized companies, many of which could not operate during the lockdown - so they have access to credit and survive through the crisis.

- **Other risks**

  The current oil price war between Russia and Saudi Arabia has pushed the price of oil to as low as USD 20 per barrel – a level last seen before the turn of this century. This creates solvency issues for the U.S. shale gas industry - an important sector of the U.S. economy and high yield market – as it needs much higher prices to survive.

  Half of the investment grade market is BBB. If even a small percentage of these companies are downgraded to BB+ (junk status) due to the current economic crisis, many pension plans and ETFs will be forced sellers, which could trigger a wide-spread sell-off with repercussions on the entire bond market.

- **Things to do NOW**

  Social distancing, self confinement and immense caution.

  If you have leverage, reduce it.

  If you cannot stand the volatility, take advantage of the occasional rebound to trim your holdings.

  If you do not need liquidity in the next five years, keep patience and do not sell everything. Diversify among regions and asset classes. Use the large selloffs to add to quality and themes that will benefit from the pandemic such as technology and healthcare.

  So far every crisis – regardless of how dreadful it felt when in it – did get resolved.

  We have extremely low interest rates, very low oil prices, comparatively low equity valuations, renewed massive QE, huge fiscal packages and support programs around the world. Equities remain liquid and are – with care and caution – still the most appealing option.

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