Monthly Commentary 3rd April 2020

Last month, we began the commentary by saying that "February was a horrible month for risk assets". Compared to March, February was mild. March saw much larger falls in the global equity markets (-13% as measured by MSCI World), but also huge falls in investment grade bonds (about -7%) and energy (-54% for US Crude oil). Even gold did not manage to make money. The only major asset that did very well was US Treasuries (+3.3%), which showed its true "safe haven" status. The USD was up almost 1%.

Is it different this time?

We are living an unprecedented time of turmoil and real economic devastation like never before. Or are we? While we are in the midst of this crisis, we cannot tell what the future holds. But past crises were also unique, like the housing and credit crisis of 2008/9, and the technology bubble in 2000. Yet markets have always found a bottom and recovered from these "unknowns"

Who saw it coming?

Some investors will claim that they saw the coronavirus-induced bear market coming, just like there are those who say they sold ahead of the housing bubble or the dotcom crash. Some may even be telling the truth. But there were plenty of excuses to take profit over the last decade, during what became the longest bull market in history – the trade war, the European debt crisis, the high valuations to name just a few. Up until a month ago, acting on them would have cost you.

When assessing the situation from a manager's point of view, some perspective is needed: Seven weeks into the virus the markets hit an all-time high (Feb 19). Already in early February China was in complete lockdown and hundreds were dying every day, yet western markets collectively decided that they should not worry.

Surely hindsight is a great tool but it's important to know how the investment world (including Elgin) "strategized" a month ago. Bank of America Merrill Lynch is the world's biggest wealth manager. They are credible and very well regarded, having thousands of top analysts and highly qualified investment professionals. It is worth looking at their outlook from their monthly Research Investment Committee on Feb 11th, five weeks into the Coronavirus.

While they mention the coronavirus crisis in the first line of the report (**and 12 more times in subsequent pages**!), their suggestions, with a 3-6 months view were:

“Bullish US Equities”

Region	Ticker	Core view (3-6 months)	Rationale
Equities	**MXWD**	**Bullish**	
North America	MXNA	Bullish	BofA's S&P 500 target for YE 2020 is 3300 and 2020E EPS is $177. Savita Subramanian believes moderating trade risk, signs of stabilization in macro data and neutral equity sentiment are supportive. She also sees the potential for several tactical shifts, including Growth/Momentum to Value, US to ROW, large caps to small caps. OW: Financials, Consumer Discretionary, Industrials and Utilities.

“Bullish Energy”

Commodities	**MLCXTR**	**Bullish**	
Energy	MLCXENTR	Bullish	Francisco Blanch projects Brent to average $60/bbl, and WTI to average $54/bbl in 2020.

“Bearish Government bonds”

Fixed Income	**GFIM**	**Neutral**	
Government	W0G1	Bearish	*US*: Mark Cabana expects 10y Treasury rates to trade in ranges around 1.80% for most of 2020. *Europe*: Ralf Preusser sees 10y Bund yields -40bp (20bp lower than current forwards) as a more likely center of gravity in 2020

“Bearish Cash”

Cash	**G0B1**	**Bearish**	

Source: BofA Global Research

So far, their Feb 11th suggestions appear to have been COMPLETELY wrong on all four conviction calls. This does not make them bad managers. Unfortunately, the speed at which it all happened made it difficult for any manager to go underweight equities and oil, and overweight cash and government bonds. One should also note that despite the 20-30% falls in equities, the percentage of total equities that were sold was not much more than 1%.

In the end, as serious and frightening as the market and economic setbacks are, if one holds solid funds and securities, they will eventually bounce.

Below is the latest thinking from Merrill in bullet points. While you can take it with a pinch of salt, much of what they say is universal and applicable, and we agree:

Why stay invested?

Not staying invested means missing most of the long-term market upside...it's simply too difficult to time the market. A strong impulse to hide out in cash is often a sign that a buying moment is near:

- *We know that the best days often follow the worst, and this has been the sharpest drop into a bear market in history;*
- *Since 1929, in the 24 months following a bear market, S&P 500 total returns have averaged 20%. Excluding the Great Depression, the average gain was 27%*
- *Since 1931, an investor who missed the 10 best days of each decade made 91% in equities. Staying invested meant earning 14,962%;*
- *In the 2010s, missing the 10 best days meant gaining only 95% instead of 190%;*
- *Over any 10-year period, the odds of ending with equity losses are just 4%;*

We are happy to say that only a very small fraction (4 to be precise) of our clients have asked for their portfolios to be liquidated. Three of them want to wait until "market prospects are better" before they tell us when to get back in. We wish them a lot of luck, because that is what one needs to be able to time the markets. We do not know when the bottom will come. What we do know is that a surprising share of a new bull market's returns pile up in the very early stages, when people are most fearful. If one waits for happy headlines and hopeful government statistics for a clue on when to pounce, they'll be too late.

If the last month truly convinced you that you had too much money in stocks to sleep well at night then take your lumps and dial back your risk permanently. But if you're merely waiting for a sign that it's safe to buy again then just hold your nose, increase your allocation to equities, and learn to love bear markets {from the Wall Street Journal}.

So, if one holds cash that they do not need for the next few years, while counter-intuitive in the midst of a huge crisis, they could do worse than investing it now. If they liked the Dow at close to 30K on February 19th, then the Dow at 20K would be quite enticing…

As a wise man once said: "*Don't sit on cash all the way down trying to find that perfect day. That doesn't turn out so well. The person who put some cash in the market in January or February of 2009 may have felt bad in March or April of 2009, but they didn't feel badly in 2019 when they looked back on that trade compared to friends who stayed out*."