ARIA | CAPITAL

INVESTMENT INSIGHT

A weekly look inside the investment world.

> ***All labour that uplifts humanity has dignity and importance and should be undertaken with painstaking excellence.***
> *Martin Luther King Jr*

Friday, 1 May 2020

In this week's Investment Insight

A fixed income insider's perpspective
Traditionally investors turn to bonds when equity market volatility spikes. Sometimes, the expected inverse correlation between the two asset classes breaks down in the shorter term, but during the recent volatility it has served investors well. That's not to say it's been all calm and collected in bond markets while equity investors have fretted, far from it. Liquidity dried up substantially, even in major government bond markets, until central banks came to the rescue. In *The Insight Track* we get a fixed income insider's perspective on what it was like operating through the challenges presented during the height of the coronavirus-driven volatility.

The score so far
We are about one quarter way (in terms of number of companies reporting) through the S&P 500 Q1 earnings reporting season. You could be forgiven for anticipating a bloodbath, but the reality is far from it. Of course much of the coronavirus impact will be felt more in Q2 than it was in Q1, but it's worth bearing in mind, albeit subject to material uncertainty and probable revision, that the consensus earnings growth outturn for the full year is still in positive territory. In *Pic of the Week* we take a snapshot.

Newswire
Some interesting nuggets from this week's newswires.

Market view
A visual snapshot of recent market performance.

The Inside Track: A fixed income insider's perspective

Mike Riddell and Kacper Brzezniak, managers of the Allianz Strategic Bond fund knocked it out of the park in March. Doing so required an approach that was fleet of foot and well-timed. Here's how they chronicled their exploits through the height of the coronavirus-driven volatility.

The global cross-asset sell-off continued headstrong into March, as social distancing increasingly became the norm in Europe, the US, India and elsewhere as governments across the globe sought to limit the spread and damage of the virus. One significant bright spot in March, however, was the gradual normalisation of economic activity in China as the country appeared to be coming out the other side of the crisis towards month-end. From the 23rd of March, riskier assets also enjoyed a moderate bounce in stark contrast to the toil they endured for most of the month.

A notable feature of the widespread market turmoil in March was the continuation of significant liquidity shortages throughout large parts of the market. With a partly self-reinforcing effect, investors rushed to sell any parts of their portfolios they were able to liquidate close to a mid-price to raise cash. This lack of liquidity even spread to core developed market government bonds before central banks globally stepped in to provide much needed liquidity. It was this broad-based liquidation, rather than the consensus narrative of fiscal issuance fears, which drove the government bond selloff and associated curve steepening. With the exception of ECB President Lagarde's blunder on the 12th March, where she stated it was not the ECB's role to "close the spread" in sovereign debt markets, central banks acted decisively in March to restore some market calm.

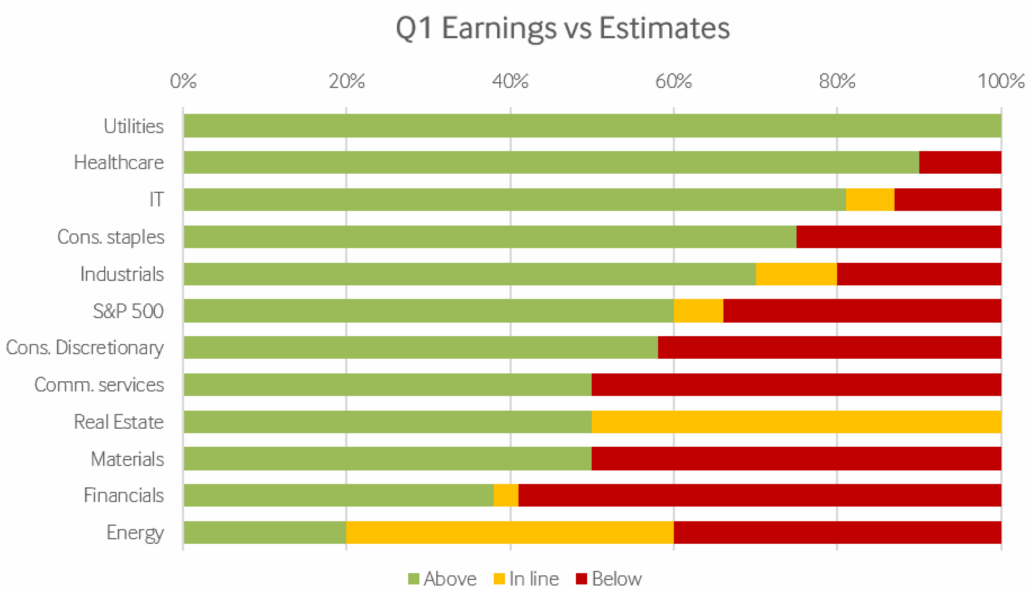
The US Federal Reserve in particular took aggressive action early, announcing a 50 basis point cut in the Federal Funds Rate on the 3rd March, before cutting a further 100 basis points mid-month to near zero. As part of this 'bazooka' response, the Fed also announced further monetary measures, including extending dollar swap lines to help ease liquidity issues throughout the global economy. Perhaps most significantly was the open-end purchase programme from the Fed, which for the first time included corporate bonds in addition to treasuries and mortgages.

The Bank of England was also decisive in announcing significant monetary stimulus and cutting the base rate to its effective lower limit of 10 basis points. In addition to monetary measures, governments across the globe announced varying fiscal responses to combat the virus, the most significant of which was the US' $2 trillion fiscal package. This increased issuance globally will largely be consumed by respective central bank bond purchase programmes however.

The range of supportive monetary conditions introduced by central banks, together with the pricing in of an economic downturn, saw credit spreads approach attractive levels in the latter part of March. Whilst the global economy is now almost certainly headed for recession as a result of the impact of COVID-19, the significant monetary and fiscal stimulus injected by global authorities provides the potential for a sharp bounce-back in economic growth once virus-induced shutdowns are gradually lifted. The risk to this scenario, however, is a significant second wave of the COVID-19 virus later in the year. This, together with the exact timing of any potential global economic bounce back, remains largely unknown.

Pic of the Week: The score so far

With over a quarter of the S&P 500 Q1 earnings reports filed, as the chart shows it hasn't by any means been all bad news. There have been two overriding but distinct factors giving rise to the disparity between winners and losers, *viz.* coronavirus and oil prices. Undoubtedly there is far more uncertainty in respect of the second quarter, but it's worth bearing in mind that outturns will vary radically in the current environment according to the sector they are in. As in Q1 so far, some - healthcare, IT, staples - will fare admirably as a result of the "new normal" whereas others - consumer discreitionary, real estate, energy - will unquestionably struggle.



Newswire

...on Monday
Stock markets rally as an easing of quarantine measures in several countries improves risk sentiment.

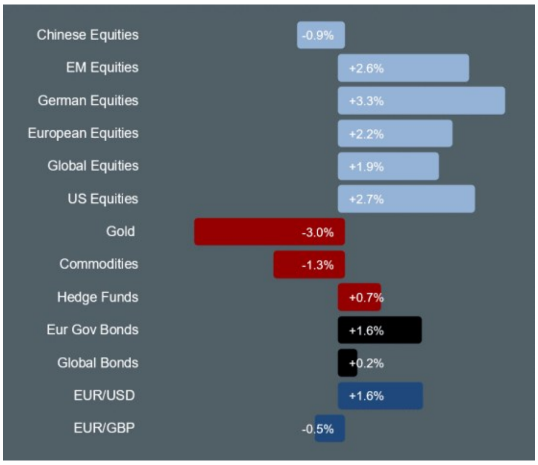
...on Tuesday
Shares in Google's parent Alphabet rose sharply in after-hours trading as the company reported better than expected Q1 results.

...on Wednesday
The US Commerce Department announces an annualised 4.8% fall in Q1 GDP.

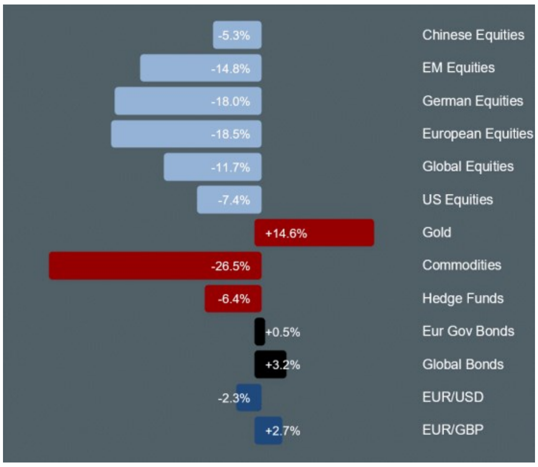
...on Thursday
Royal Dutch Shell cuts its dividend for the first time since World War II, reducing it by 66%.

Market View

Last 7 days (€)



Year to date (€)



Aria Capital
66 Fitzwilliam Square, Dublin 2, D02 AT27, Ireland
t: +353 1 6854 100
e: research@aria-capital.ie
w: www.aria-capital.ie

Important disclosures
Aria Capital Limited is regulated by the Central Bank of Ireland.

Financial data is provided by Infront and Aria Capital. All values are indicative only and should not be relied upon.

Investment Insight is prepared for information and discussion purposes only; it does not constitute investment advice or an offer to buy or sell securities. No investment decisions should be made without seeking appropriate professional advice.

This document may not be reproduced in whole or in part without Aria Capital's permission.

© Aria Capital Limited 2020. All rights reserved.