Investment Talks – Impact of Coronavirus on Economy and Markets
## Assessing Coronavirus Impact

### Degree of severity

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<th>Low</th>
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Could coronavirus lead to a global recession?

Central scenario: deep yet temporary contained shock (2020-ranges)

Risk Scenario: protracted stress, longer lasting impact

What are the real risks for European economy?

- Contracting GDP in Q1 and/or Q2 becomes the base case.
- Italy, Germany, France may likely face GDP contraction during H1, with different timing.

We expect Central Banks to do "whatever it takes" to stabilise the situation

Central banks are concerned by:

- The drop in inflation expectations
- The risk of lack of liquidity for companies due to a sudden slowdown in activities and tightening in financing conditions

Fed:

- 3 additional cuts
- Resumption of the QE (it could include IG corporate bonds)

ECB:

- The positive impact of another rate cut is not obvious and the ability to cut rate further is limited.
- Liquidity injection is the most likely option
  - Increase the size of its asset purchase program via raising the 33% issue share limit
  - Favor corporate debt purchases
  - Provide banks with more liquidity facilities and target SMEs.

Surprise rate cut by the Fed, followed by the BOE

What are markets pricing in at the moment?

YTD performance and potential 2020 outcomes from current levels (c.l.)

- Performance from 31-12-2019 to 11-03-2020
- V Shape from c.l.
- U Shape from c.l.
- L Shape c.l.
- \ Shape from c.l.

How could investors play the current market phase?

**Cross-assets**

Tactical risk reduction and prepare to re-enter

More **conservative risk allocation**, especially in equities (negative on EU equity tactically and slightly negative on US equity), **neutral on EM equity** and considering some **protection in credit**. **Positive on duration** and hedging to try to protect investors’ portfolios.

**Equities**

Exploit dislocation to add to main convictions (cyclical value)

Recent sell-off reflects downside risk to economic growth. Search for **areas of resilience in equity** (income/dividend space) and **watch for opportunities in cyclical stocks** (quality/value in Europe and US).

**Bonds**

Selective in credit and focus on liquidity

Markets are re-adjusting on a darker economic outlook. After this, and with core bond yields at their lowest level ever, **the search for yield will return**. Spread widening may offer attractive entry points in credit with good fundamentals. **Be selective, focus on liquidity**.

**Emerging markets**

Selective, focus on domestic stories and new themes

Short-term pressure on EM equity, debt and EM FX. **Opportunities in country-specific stories**. EM equity is attractive and could bounce back once the situation stabilises. Focus on domestic demand stories and new themes such as the Silk Road.

References & definition

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Blu histograms: YTD returns, including future today.

V shape (green): covid19 shock confined in Q1 in China with global spillovers via trade and supply trade disruptions. This was our initial hypothesis in mid-February. Today, we believe the outbreak in Europe leave this scenario. This was a game changer: it is unlikely Europe will show same resilience as China on the monetary and fiscal front. However, should this be the case, the upside from current levels is on average higher than 20%.

U shaped recovery (light green): this scenario underlines a V shape recovery in China and a mild recession elsewhere, with a very contained number of countries entering a recession (likely Italy, Germany). This scenario sees a recovery in H2 and sees an upside from 5 to 10% on equity front. Includes prompt global action from monetary and fiscal side to move back to late cycle in H2.

L shaped: global growth structurally downward shift with CBs active in preserving liquidity in the market and fiscal measures to help on supply. This is the scenario the markets are pricing in and includes credit crunch risk and depressed inflation expectations.

Global Recession: worst case scenario.
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