

# Potential Impact of the Coronavirus to Capital Markets

30<sup>th</sup> January 2020

## Latest Development

- The Global financial market has taken a dip in the wake of the novel Coronavirus outbreak as investors become nervous about a world-wide epidemic.
- Coronavirus is a wide range of viruses that usually infect animals but can spread to humans. On 31<sup>st</sup> December 2019, China alerted the World Health Organization (WHO) to several cases of pneumonia in Wuhan, a port city of 11 million of people in the central Hubei province.
- While the WHO last week deemed “an emergency in China,” it has yet to issue an official global alert.
- As of this writing, we have nearly 4,500 confirmed cases and 106 deaths, the vast majority of whom are in China.

	SARS (Final)	Wuhan (Current)
Number of confirmed cases	8,096	7,837
Number of deaths	774	170
Fatality rate	9.60%	2.10%

## How different it is now as compared to the past?

- Infectious disease outbreaks tend to roil the stock market and send stock prices lower, but the losses are typically temporary.
- This epidemic is expected to affect businesses and financial markets, but it may ultimately have more impact on sentiment than a lasting negative for the economy. For example:
  - I. The SARS outbreak back in 2003 saw the global stock market tumble but stocks recovered once the outbreak was contained. The S&P 500 dropped approximately 10% from the start of the year until mid-March but finished up more than 26% for the whole year.
  - II. Similarly, Hang Seng index (15 Nov 2002-12 Mar 2003) fell about 10% before recovering. The index ended 2003 up 35% while the MSCI Asia-ex closed 40% higher despite the high death toll and lingering economic weakness due to the epidemic.
- To be clear, China’s response to the novel Coronavirus outbreak has been proactive and transparent, in contrast to its slower reaction during the spread of SARS.
- In addition, with the world far more linked than before would allow mitigation to be performed earlier and more effectively.

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## Economic Impact

- The outbreak, which comes just after Washington and Beijing signed a partial trade deal, creates uncertainty for businesses that manufacture and source materials in China.
- History has guided the turning point for sentiment will come if the vaccine is invented and escalation of the virus decreases.
- The negative sentiment in the short-term will affect businesses particularly in the consumer, transportation, restaurant, tourism, and retail sectors.
- That said, with the online channel now accounting for 20% of total retail sales, this can increase to partially offset the impact on the overall retail sales number.
- Commodities such as oil will also be affected in the near term amid concerns of slower global growth and lower demand.

## What Could the Chinese Government do?

- We expect the Chinese government would provide “targeted fiscal policy support” and accommodative money policy just like the SARS outbreak back in 2003.
- Globally, we expect the interest rates to remain low with China expected to cut Loan Prime Rate (LPR) and Reserve Requirement Ratio (RRR) further.
- This should provide support to the market even if the global PMI recovery gets affected due to this epidemic.

## Investment Implications

- The novel coronavirus has a long incubation period of up to 10 days and can be spread before symptoms are apparent, which suggests the situation could prolong.
- This is also coupled with the ongoing uncertainties such as Brexit, US Presidential election and Impeachment Trial, in which investors should expect a short-term bumpy ride in the stock market.
- It is important for investors to hold a globally diversified portfolio with diverse asset classes depending on their respective risk profiles.

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## Strategy Going Forward

### Asia Pacific Region:

1. A market sell-off on the back of such epidemic usually offers great buying opportunities.
2. We would be buying into structural names with good management and strong business models.
3. Even though e-commerce may be a relatively more resilient sector with Chinese consumers choosing to spend more time at home and demand for online shopping may increase, stocks of these companies are likely to also be sold off indiscriminately in a knee-jerk reaction.
4. We will be adding companies that are capable to lead in the growing consumption space in China.
5. We also like companies that are emerging as the key players in the fourth industrial revolution.

### Malaysia:

1. We retain our overweight position on Malaysia as it is a low beta and defensive market during this period of uncertainty.
2. We maintain our barbell approach on high yield sectors like REITs and utilities and increasingly favour cyclical growth sectors like banks, plantation, oil and gas, and the technology sectors.
3. On the other hand, we believe tourism related sectors such as airport and aviation will be affected by the sharp fall in Chinese tourist arrivals in the near term. This would be compounded by the regulatory uncertainty involving the implementation of the Regulated Asset Base framework.
4. That said, we are underweighting the airport and aviation sectors.
5. Glove and healthcare stocks would be re-rated in the near term driven by sentiment as well as short term spike in demand.

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