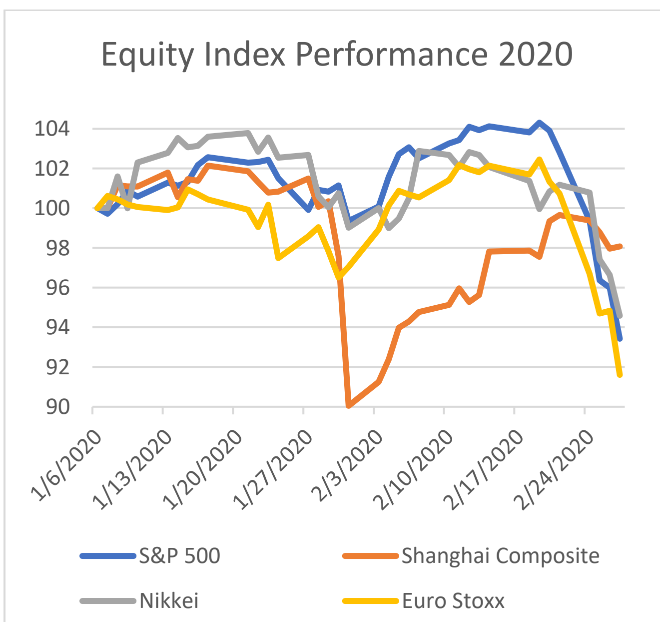
RockCreek

March 9, 2020

Is the New Coronavirus Winning? Markets Seem to Think So

Markets ended last week in turmoil – and look set for further chaotic moves. Have policymakers shot their bolt? We think not. But as we explain, they need to up their game dramatically.

Last week began with the United States and other major governments taking the new COVID-19 threat seriously. In short order, the Fed implemented an emergency 50 basis point cut, the IMF and World Bank promised billions of dollars to support weaker countries, and even the notoriously divided U.S. Congress pulled together to pass an emergency spending bill focused on beefing up health resources. Markets were not impressed. Recently released reports of good news from February, a bump in employment in the United States and revived demand for Germany's factory goods, did not appease investors. The 10Y ended below 1% for the first time ever. Yet none of that seemed to matter as coronavirus continued to be the only thing on the mind of every investor. While the S&P and MSCI World finished the week in positive territory, interesting technicals are signaling a possible bottom. All of this adds to the uncertainty as we begin a new week.



It is little surprise that markets are so unhappy. The political response to COVID-19 has been close to disastrous. The last week has shown just how serious the virus threat could be at the same time as it has become clear just how unprepared we are to address it. The United States, with all its resources, was not able (or willing?) to roll out the mass testing needed to understand and control the virus even after its symptoms and severity were known. More than two months after the initial outbreak in China, there remains a shortage of protective gear for health workers, of ventilators for patients, and of clear guidance or protocols from the government on how best to avoid infection or what to do if you become sick. Two years of cuts in spending have left the CDC weakened. Cases of so-called "community transmission" exploded in the past week, showing that rapid and widespread illness is an inevitability, a fact the CDC had tried to warn the public of. Increasingly, companies, individuals, local communities, and governments are taking matters into their own hands and deciding – with little guidance – how to respond.

Now is the time for enhanced, coordinated global action. A strong, unified response is the only way to restore calm to markets and societies more broadly.

The public health threat must be top of mind. Governments are right to look first to protect their citizens. School districts, likewise, should look after their young charges. And a cascade of travel restrictions and conference cancellations shows that companies are also looking to do their part in protecting employees and limiting the spread of the virus. What more can we expect?

4 key points, as we enter week three of market turmoil.

1. *This is not going to end quickly.*

   The past week has – sadly – demonstrated that the United States was ill prepared for the threatened pandemic. As China's experience showed, swift action to contain infection is essential. Denial and ignorance are dangerous.

   Information may not have been deliberately suppressed in the United States as it was in China. But the call to action that should have sounded two months ago, when news of the novel virus was first reported, went unheeded for weeks. As a result, we still have far too many unknowns. The failure to support testing for the virus was particularly foolish. Without adequate and widespread testing in the United States, we do not know how far the virus has spread.

   Now that medical professionals are trying to treat patients and suspected cases, it seems that many of them do not have the training in infection control needed to safeguard themselves and their communities. This means that COVID-19 has already had plenty of opportunity to spread. It will require a vastly bigger testing operation than what is in place to date to understand how far the virus has spread.

   As market participants know all too well, the worst thing is ignorance. When you do not know how bad things can get, there is no floor.

2. *As key information becomes available, medical and scientific experts should guide the public's actions: markets and governments included.*

   Experts have advised that some basic practices can go a long way in limiting transmission. Handwashing is important to curb the spread of COVID-19. Keeping a "social distance" from one another is also recommended. Staying away from work and school when you don't feel well is crucial. Panic buying – especially of goods like face masks that are needed for health workers – is unhelpful.

   To better address our response, we need to know how infectious – or transmissible – the disease is, whether it spreads before symptoms show, and what the mortality rate is. Estimates for all these elements have varied substantially in recent days. When the numbers settle down, we will know whether – as we said last week – this is the big one, or a dress rehearsal.

It is critical to get a realistic guide to when treatments, or even a vaccine, could become available. That is another area where scientific expertise and clear communication, not unfounded cheerleading, are needed.

3. Policy actions cannot wait.

It is always hard to act in uncertainty, but that is what a crisis demands. We see three key areas for government action.

First, steps to *bolster the health system* are urgently needed, as Congress has now recognized. In the short term, emergency supplies of masks, infection protection equipment, and ventilators must be sent around the country to health professionals. Emergency hospital capacity should also be developed, as it was in China. We may hope that it is not needed, but better to be prepared. Training in the use of tests for the virus and in infection control is also crucial. At the same time, longer-term research and development, whether this takes place in government or private institutions, in the United States or outside, needs support if we are to find effective treatments and prevention. Scientists in the United States had a promising lead on a vaccine for coronavirus in 2016. But there was no money for the extensive safety testing that is required, so the effort died. That must not happen again.

Second, there remains a role for *monetary and financial policy*, albeit a more limited one than central banks have played since the financial crisis. The global economy is being hit hard by a supply shock, as we noted last week. But as the spillovers to jobs and incomes and profits reverberate, it will be critical for central banks to do what they can to support demand as well as to ease the likely credit squeeze on specific sectors and companies. Some companies, especially smaller ones, may find it hard to access credit. Consumers burdened by high debt may struggle to pay if they are unable to work. Easier credit conditions cannot cure COVID-19. But they can help to limit the economic damage.

Third, and perhaps most importantly, governments need to *use fiscal policy* on a much larger scale than so far envisaged. Politicians need to listen to the experts and take decisive action based on their findings. Economists, including many who have been cautious on deficit spending and tax cuts in the past, are increasingly calling for broad fiscal support in the United States and other major economies. Of course, spending and tax relief should be targeted to the extent possible to give support where it is most needed. This means legislating to put money into the hands of the most vulnerable, those who cannot afford to be laid off temporarily as events are canceled, tourism collapses and trade shrinks.

As David Wilcox points out in his useful blog for the Peterson Institute (PIIE), we need both immediate measures to address the specific consequences of this health crisis and broad and concerted support to aggregate demand to pick up the economic and financial pieces after the immediate danger passes. In the first category are federal spending to ensure healthcare provision for the millions still without it; state efforts to replace free school meals for the millions of school kids who will go hungry if their schools close; and emergency paid leave for needy parents that cannot work when schools close. The second, long-term category requires thinking big to avoid the health crisis tipping the United States into recession. Ideas include a cut in the payroll tax – temporary, perhaps – or direct rebate checks in the mail to support incomes and employment. So far, the President, his administration, and Congress have not been ambitious enough. It is great to have $8 billion spending rushed through but that pales beside the nearly $1 trillion that was mustered in the wake of the financial crisis of 2008. Most experts have concluded that the 2008 stimulus package was, if anything, too small. Let's not make the same mistake again.

4. Markets will continue to be irrational and opportunities, abundant.

As always in a crisis, financial markets are the first to price in the extreme case and the last to reward those areas that will appear stronger in the aftermath. Global investment opportunities are becoming apparent and, based on what we are seeing from the impact of coronavirus, plentiful. Throughout recent years, RockCreek invested in both public and private investment opportunities globally in the healthcare sector. What this crisis has shown is that there is an urgent need for an increase in both public and private investments in healthcare and ancillary services, especially if we are to support both an increasingly elderly and potentially vulnerable demographic. This investment can’t be temporary and must be supported by long-term capital. A RockCreek biotech company investment was already on a path to developing a potential vaccine to fight coronavirus and has accelerated its timeline in partnership with one of the largest vaccine manufacturers globally.

Outside of healthcare, more immediate consumer needs have lifted certain sectors and brought attention to areas otherwise ignored. As school districts and governments move to contain COVID-19, creative alternatives to continue learning are being explored. Online education and distance learning companies have never looked so attractive in terms of the sector’s potential in the future to be both mainstays of a typical education as well as part of backup policies. Video conferencing and long-distance communication tools are also gaining. As we continue to assess markets in the short term, we are keenly interested in ensuring that we are looking to future trends, sectors and companies that are providing what may become essential services and products in the future. These are the areas we want to be invested in for the long term.

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