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Investment Management

- Communication -

The world is currently facing a crisis our generation has not experienced before. We limit our-selves here to analyze its impact on financial markets and our way to manage portfolios.

After decades of efforts to make globalization happen the entire globe is now more interconnected than ever. Companies have globalized both their markets and their supply chains and consumers have today much better possibilities to travel between continents than they had just 10 years ago. Living standards are the highest ever in most countries. There are challenges like climate change or social imbalances. Overall, the world is a fascinating place that keeps on developing in the right direction once we take a longer time perspective on things. We highly recommend spending an hour of your life to watch the award -winning "Don't Panic" video where the positive development of the world is presented in a very forceful way. The video is insightful and entertaining. Perhaps we need both in these times.

From time to time this march forward is being disrupted. The disruption often comes in the form of a recession where the excesses built up over years in prosperous times are being cleared. Sometimes the recession is triggered when Central Banks become "hostile" and hike the interest rates making the funding costs for new projects (think new factories, highways, R&D etc) go up. The result: New projects are no longer seen as profitable and they do not happen. This puts a break on economic growth, corporate leaders and consumers alike become more cautious and that puts another break on economic growth. Voila, the recession has landed.

This time around, the situation is different (the outcome may not be so different). Central banks are extremely "friendly", and they keep their interest rates low. The trigger for a probable recession is now the coronavirus and the efforts to slow down the spreading of the virus. Across the globe politicians are asking their people to stay at home and companies to reduce their operations to protect their staff. From China (where the virus came from in January) we know that these drastic measures are what is needed to flatten the curve of newly infected people. The economic effect is of course negative short-term and something we cannot escape. We just have to go through it. In the long run neither a virus nor a recession will have a big long-term impact.

A globally connected world requires globally coordinated efforts from Central Banks and governments. We expect that to come as the US Central bank Sunday 16/03 pulled out one their big bazookas offering liquidity and asset purchases in coordination with the European Central bank. More of that will come and those powers should not be underestimated. We will all get through this.

From a pure investment perspective, we should ask ourselves: What can I do to help myself get through the situation and come out on the other side even stronger? For that we have some suggestions:

Stop checking your portfolio all the time. Daily prices do not say anything about real business value and checking your paper gains daily, and hourly fosters short-term thinking.

Stay invested. Selling your portfolio now means you may take a permanent loss of capital. Getting back into the market again is emotionally very difficult once you have convinced yourself about the idea to sell your portfolio.

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Stay invested (ctd). Edgepoint made a study on stock market performance after 10 bear markets since 1947. The weakest 12 month return after the end of a bear market was 26%. The strongest was 72% (that was after the 2008 crisis). Missing out on those gains is extremely painful for long-term returns, so stay invested. Bear markets are inevitable but how you respond to them will determine where you stand once the markets rise again.

Keep dry powder to invest more. Some of your investments for sure pay dividends. You may also have some cash reserves elsewhere. The value of that cash goes up dramatically as stock prices are falling. Simply put, you can buy more ownerships of companies for the same amount of money. Take some of that cash and buy when others are forced to sell. Those who invested in the S&P500 Index on 1st January 2009 (3 months before the bear market ended) initially had to suffer a 20% drawdown in just 3 months but ended up generating a total return of 350% by January 2020 and 280% by today. By all standards these are powerful returns generated through a period where the world has seen its fair share of challenges (US debt ceiling, double-dip risk, euro crisis, trade war, geopolitical tension, virus etc).

So, what are we doing inside ECP in the current situation?

We do our best to ensure our companies can weather the storm. Our focus on strong balance sheets is important. The companies we own have been through rough times before and we expect them to come out stronger on the other side. Some of our companies will for sure use their strong balance sheets to acquire weaker competitors, new technology etc.

Before the coronavirus started spreading, we increased our cash position. Not because we saw anything coming (we don't even spend time trying to predict such unpredictable events) but because our focus on valuation warranted to sell/reduce some positions.

We slowly put money to work in companies priced as if the world is going under. We don't believe it will, so we try to make use of the best opportunity set we have seen in 10 years. We always build our positions slowly taking valuation, quality, and liquidity into consideration. So far, we have added 4 new businesses to our portfolio.

We do respect the pain of seeing the value of our investments go down. After all, we want them to go up and generate wealth. We feel the same pain as our dear customers, since we are invested alongside you. We eat our own cooking so to say. As professional money managers we have seen crisis situations before, and we are willing to bet that neither the virus nor a recession will make the world go under. We also know that the best opportunities are created when you are able to cut-off your emotions and be a careful buyer when others are stressful sellers. And that is just what we are doing, instead of watching the daily prices moving.

Stay tuned, we will update you as we move forward.

Kind Regards,

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