

Coronavirus (COVID-19)

February 29, 2020

In January, the World Health Organization (WHO) declared the coronavirus outbreak a public health emergency of international concern. As the outbreak spread across Europe and into North America in a more meaningful way this past week, global equity markets reacted accordingly – off nearly ten percent for the week. The bond markets – generally a haven – provided a little shelter, posting a positive return of nearly one percent.

The growth and spread of this virus have caused great concern globally for people and their governments. Investors now confront a fear of the unknown. Uncertainty causes anxiety and investors prefer predictability. We believe fears about market impact are overblown. Let's begin with a brief primer on the virus itself and then analyze the possible ramifications.

Coronaviruses are a large family of viruses which may cause illness in animals or humans. In humans, several coronaviruses are known to cause respiratory infections ranging from the common cold to more severe diseases such as Middle East Respiratory Syndrome (MERS) and Severe Acute Respiratory Syndrome (SARS). This most recently discovered virus causes the disease coronavirus 2019 or COVID-19.

As of February 24, there have been 79,524 confirmed cases of COVID-19, 2,942 of which resulted in deaths (just 107 outside mainland China).¹ Fifty-seven countries confirmed cases of the virus, 62 in the US and 14 in Canada. In the chart below we take a look at how COVID-19 (identified below as SARS-CoV-2) compares to other outbreaks.



Chart 1: Size of bubble represents the number of cases of respective disease. Sources: WHO and CDC.

¹ As of 3:00 pm PST, February 29, 2020, 85,964 confirmed cases worldwide and 2,942 deaths worldwide, 107 of which have been outside mainland China.

While COVID-19 has not run its full course, to date it has not proven as prolific nor deadly as others. Influenza, the common flu, has inflicted over 29 million people this flu season resulting in 16,000 deaths – in the U.S. alone.

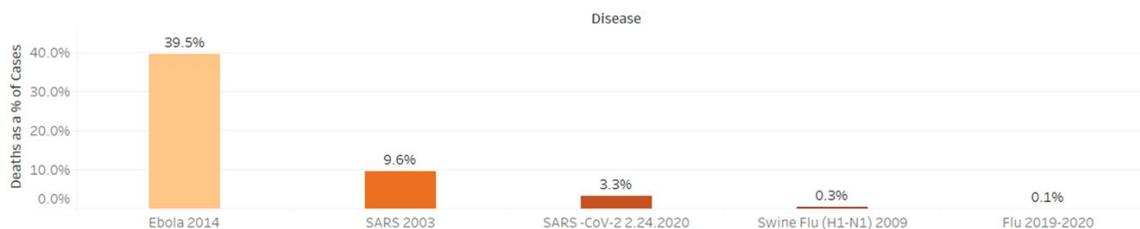


Chart 2

The potential impact on global commerce has been the subject of much debate and worry. Since COVID-19 was first discovered in China on December 30 of last year, factories have temporarily shut down to stop the spread of the disease, causing disruptions in supplies of goods needed to manufacture other products (the supply chain). The fear of going out and contracting the virus has also led to a significant slowing in consumption of goods, entertainment, and travel.

China has become more and more important in the global economy, both as a supplier and consumer of goods and services. The global economy has changed since 2003 when the first SARS outbreak occurred. China now accounts for 16% of global GDP, up from 4% back then. And, it is the world's second biggest importer, so any weakness, however temporary, is felt far and wide. Aside from the aforementioned supply chain, China's tourists spend \$250 billion a year on overseas travel, and they are staying home...for now.

This has no doubt impacted current quarter economic output and could also impact next quarter. We see economic growth being lower over the course of 2020. Once this runs its course, spending should rebound quickly and sharply - pent up demand will be the key driver. Looking forward 12 to 36 months, economic growth and earnings forecasts are not impacted. Therefore, companies are cheaper today relative to future earnings than they were just one week ago.

Despite the markets' sudden downturns, now is not a time for panic. This short-term disruption is happening at a time when we're seeing more and more opportunities in high-quality companies at very reasonable valuations. We are monitoring the situation closely and, as you've come to expect, keeping perspective on the events and the longer-term implications for you and your investments. Clearly, COVID-19 is causing disruption to the global economy, but this will pass.

Charts 1 & 2: CDC estimates that so far this season there have been at least 29 million flu illnesses, 280,000 hospitalizations and 16,000 deaths from flu as of the week ending February 5, 2020. U.S. flu season 2019-20 runs from October 2019 to May 2020. All data reported by U.S. Public Health labs. Coronavirus (renamed SARS-CoV-2), Outbreak was first reported in December 2019. Swine flu (H1-N1) 2009: (H1N1, the number of deaths reported by the WHO are models that estimated the actual number to be in the range of 123,000 to 203,000). Sources: WHO and CDC.