March 18, 2020: INVESTOR INSIGHTS – Coronavirus

As news of the spread of COVID 19 virus across the world assaults us every day across virtually every media outlet it is easy to understand the increasing level of panic that is gripping people from all walks of life across the globe. However, during periods of such volatility it is essential that we avoid panic and instead step back and review the situation through the lens of logic.

While even the most seasoned investor was surprised by the scale of the global stock market correction over the last three weeks – we still need to remember that our investments were made to build value over the long term and crises like the Covid 19 typically have only shorter term consequences.

In 2008 the global financial system was nearly undermined by the sub-prime mortgage crisis, which was caused by reckless lending practices and rating agencies that “dropped the ball”. As a result, it took years before global financial markets fully recovered. The current Covid-19 crisis is not a financial system crisis, but rather an exogenous or external shock. It is important for investors to differentiate between exogenous shocks, or those shocks resulting from an external cause to financial markets versus financial system-based shocks, or those shocks resulting from causes in the local economy. The Covid-19 shock is exogenous and not system based, so therefore the recovery is expected to occur sooner and be more robust.

Over the last 19 years we have had 12 epidemics including SARS in 2003 and MERS in 2013. Following the previous 12 epidemics the drop in stock market values was followed by an average recovery of 13.6% 12 months later. On February 19th, less than a month ago, the S&P 500 Index closed at 3,386.15, the highest close in history. At close of trading on March 18th, the S&P 500 Index had declined to 2,398.10, or 29.18%. We anticipate continued volatility in international markets as Covid 19 related news and government and central bank reactions change investor expectations.

While past performance is no guarantee of future performance, in the past such market declines are usually followed by sizable recoveries.

What does this mean for Bahamian investors? The impact on local equity and debt markets will depend on the severity and duration of Covid-19 virus’ impact on our tourism sector. With the cancellation of all cruise ship travel for at least the next thirty days and with air travel and hotel occupancies also expected to be severely impacted, it is expected that there will be a sharp decline in tourist revenues for weeks if not months. Recognising that the Bahamian tourism industry is already struggling to deal with the impact of Hurricane Dorian on Abaco, it will be essential that measures are taken to minimize the impact on Bahamians whose livelihoods are directly dependent on the tourism industry. It is fortunate that the Bahamas has sufficient foreign reserves and access to global debt markets to sure-up our foreign reserves if needed.

While the loss of tourism revenues will negatively impact The Bahamian economy and it is expected that the financial performance of the firms listed on BISX will be similarly impacted in the short-term, we do not expect negative medium to long-term impacts that would likely justify significant declines in share prices on BISX.

Let's think about the companies listed on BISX. The demand for supplies, some essential some not so essential, has and will continue to benefit food stores like AML Foods and Commonwealth Brewery. Also, as in the US, technology and telecommunication firms like Cable Bahamas/Aliv will benefit. Demand for cable/internet access and data will increase. Also, in the case of Cable Bahamas, they recently generated approximately $200 million in cash from the sale of their US subsidiary. We have five local banks listed on BISX and if needed they can decide to provide lenders with the option to make interest only payments for several months. This will not impact profitability while reducing new delinquencies. Regarding the three insurance companies listed on BISX, keeping one's health and life insurance policies current will be a priority for most of the insured. During a medical emergency, demand for health care services increases and Doctor's should benefit. Regarding FOCOL, their profitability increases when oil prices decrease, and the price of oil has plummeted. Also, like food, demand for gasoline remains somewhat stable during economic downturns. As such, we are not of the view that the COVID-19 crisis will spell doom for local stocks.

The RF Prime Income Fund's (PIF) top ten investments include: Government of The Bahamas (14.2%); Cable Bahamas (13.8%); NAD (13.0%); Be Aliv (13.0%); RF Holdings (4.3%); CARIBCO Limited (4.3%); RF High Yield Income Fund (4.0%); Fidelity Bank (4.0%); APD Limited (3.3%); Lyford Cay School (2.6%). We are of the view that all these issuers are stable and that the PIF provides risk averse investors with a prudent option over the next few months and beyond. Also, most of the local issuers of corporate debt and preference shares have strong balance sheets we expect that they will be able to meet their obligations.

We all need to be prudent regarding our physical health and financial health over the next few months. We realise that these are difficult times and there is a high level of uncertainty as to the future impacts associated with the spread of Covid 19. The team at Royal Fidelity is here to assist you during this trying period and we would welcome the opportunity to discuss your investment concerns.

Together we will weather Covid-19 and emerge stronger for it.

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With over 20 years of experience bringing wealth management services to the Bahamian people, Mr. Slatter is an expert in wealth creation and managing risk. He holds a Master of Economics degree and a Master of Business Administration degree from York University, and is a Chartered Financial Analyst Charterholder.