Coronavirus and portfolios: We’re not waiting for a vaccine

As active managers, the Antares Equities team meets every day to discuss and challenge our views on stocks and the market. It was all-hands on deck for the February reporting season (where pleasingly many of our companies had good results) but it quickly morphed into the coronavirus crisis.

As the crisis has unfolded we have changed our base case outlook for global and Australian growth and made a number of changes to our portfolios.

Pre-Virus
Before the coronavirus outbreak, we expected the global economy to accelerate into the back end of 2020 as global manufacturing data (PMIs) turned around, the US China trade war subsided and the peak of Brexit uncertainty had passed. The US economy appeared strong and globally consumer confidence appeared to have improved. Although the outlook for the Australian economy was weak, there were some positives as house prices rebounded strongly and the Reserve Bank had indicated a willingness to cut rates if needed.

Share markets were at historically extreme valuations, supported by low global interest rates. Growth stocks in particular were pushed to ever-higher multiples.

Reporting season saw generally weak results with more earnings misses than beats and an overall bias to guidance downgrades. This dampened the outlook and saw some stocks marked down, but any impact has now been overwhelmed by the outbreak of the coronavirus.

The Virus spreads – can we immunise portfolios?
The onset of the coronavirus has caused us to re-think our base case for growth. There are still many unknowns and the market has fallen by well over 10% – a lot of bad news has already been priced into the share market. And we are confident that the lower interest rate environment will persist for some time.

However, we have identified areas that we believe remain high risk including:

- Companies with suspect balance sheets (eg high debt levels) where cash flow is at risk of disruption.
- Companies where a critical supply chain may be dependent on one source and is disrupted. However, as China returns to work it is possible for a rebound in stocks that might have been sold off in this category that can show they can safely source product).
- Earnings risk in stocks which are still trading at very high price to earnings multiples.

Hence we are turning our attention to balance sheet strength, liquidity, inventory levels (stock turn) and re-financing risk. If the coronavirus persists it may bring some of these issues to the fore.

What have we done?
Essentially, across our portfolios we have introduced new stocks that have fallen materially below our valuations in the sell-off. And we have reduced others that we feel will have a more challenged operating environment given the economic slowdown or that could display some of our concerns about balance sheet strength and liquidity.

Additional strategies across some portfolios have included:

- Investing some of our cash positions into stocks;
- Adding to some of the cyclical, coronavirus impacted stocks as we believe their valuations are now attractive from a long-term perspective;
- Adding non-directly impacted stocks (eg we’ve added Coles because its price fell despite a positive earnings result); and
- Increasing portfolio diversity by adding a range of stocks in different sectors with different attributes given we are investing in a period of uncertainty.

With such an uncertain and fluid situation we continue to diligently monitor, analyse, and discuss news and developments for markets and companies at our daily meetings. And we continue to actively manage our portfolios, identifying opportunities that we believe best position them for long-term growth for our clients.
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