Prague, 30 March 2020

Commentary on Current Situation Facing Financial Markets

Have the equity markets already identified their bottoms? Similarly as during the several past weeks, the last week was very active viewed from the angle of the developments facing the financial markets. Although we witnessed again above-the-standard strong movements regarding many classes of assets, we could notice a certain minor calming down. Such calming down could be sensed both in respect of bonds (namely, in a moderate reduction of both purchase and sale spreads, narrowing of differences between yields of sovereign and corporate bonds or in increases of the prices of corporate bonds), as well as in respect of equities whose volatility decreased by approximately 20 percent in comparison to the maximum values reached in the previous week. Equities ended up the entire past week with solid gains, free of any significant fluctuations, and they have probably begun to look for their bottom. Since the beginning of the year, purely equity indices had been losing more than 20 percent; nevertheless, in the case of balanced strategies complemented with bond instruments, such losses have been restrained, namely, in the range of lower units of percent points.

Why did markets strengthen last week? Primarily, it was due to the approval of a package of fiscal measures in support of households to the tune in excess of USD 2 trillion by the U.S. government and the U.S. president. Yet another reason was represented by adjustments of the portfolios of American open-ended funds, which began to increase the ratio of equity positions at the expense of bonds. Also, some hedge funds began to close down their short positions.

The FED former boss Ben Bernanke granted a relatively positive interview to CNBC, where he said that the current situation rather resembled a snow storm than the global economic crisis of the 1930's. The former chief expects a sharp but at the same time a quick recession followed by a speedy recovery; we share this scenario also as regards our strategies. However, such recovery will depend on how quickly the infection can be contained, shops opened up, manufacturing set in motion, and the global economy re-launched. On Friday, we also heard a positive piece of news from the repo currency markets where the American banks sought loans totalling to a mere USD 7 billion, while FED offered 500 billion dollars, which indicated improved liquidity of the part of banks.

As regards individual portfolios, we complemented our dividend strategies with shares of Berkshire Hathaway of the financier Warren Buffet, which in the past managed to exceed in the long run the S&P 500 Index. It is a strong company with a strong cash position and a will to invest also in the current difficult times. We purchased the shares more than 20 percent cheaper as against the prices of this past February, and at the same time – from our point of view – on attractive valuations. Generally, we nowadays prefer mature companies with high market capitalisations and strong cash positions in our strategies.

As regards our managed funds, we have continued to moderately accumulate certain equity positions, along with partial optimisation of the equity components from a sectoral perspective; for example, shares of commodity firms sold were replaced by broader equity indices. Following the significant slumps recorded on the American corporate bonds market (two-figure losses were no exception) we also began to purchase selectively those 'cheap' bonds. Similarly, we have also reviewed some European corporate bonds and bonds from the emerging markets. As regards credit risk, such purchases have been very conservative since more than 85 percent of such purchased bonds had investment rating (Baa3/BBB- and better).

Conclusion:

- **We do not swerve from the faster return to normal scenario**, the markets may fluctuate in the coming days and week, it cannot be excluded that they would return to the minimum values recorded in the past days.
- We believe that **equity markets have already began to identify their bottoms**; this is supported by the calming down of the bond and currency markets and lower volatility.
- As against the past week, we also sense a shift in the rhetoric of certain government officers (e.g., in the U.S.A., but also in the Czech Republic) in the direction of expected restart of the economy. **The first outlines are beginning to emerge that economies could start working again**.
- Following the growth recorded in equity markets in the past week, we have been **moderately overweight** in risk instruments in tactical allocation.
- **We continue our regular investments** – **buying more high-quality shares** – see, e.g., the purchase of Berkshire Hathaway, and broadly diversified ETF and funds. At the same time, we buy **high-quality corporate bonds**. We also leave space for further potential purchases.

We keep our fingers crossed for the days to come, and we are looking forward to next week.

For the team of your portfolio managers,

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