Securing assets in a dangerous time

The pandemic has been perilous for financial markets but has not been without opportunities, say the CIOs of Sompo International and Sun Life Financial.

By Shawn Moynihan, Editor-in-Chief

The first weeks of the COVID-19 pandemic played havoc on the global financial markets like no chief investment officer has seen since the days of the Great Recession.

In March, as the threat of the coronavirus became acute, global equity markets plunged when entire economies became stalled while governments tried to contain the spread of the pandemic. One of the longest and strongest bull markets in U.S. history came to an end on March 12 when the U.S. stock market dropped by more than 20% from its most recent peak in February.

By the end of Q1, the Dow Jones stock market index had logged a more than 2,000-point drop in a single day – the biggest in its history – before falling more than 10,000 points.

As of this writing, the S&P 500 is currently up about 25% from its closing low on March 23, after falling as much as 34% from its February high – and many CIOs are still wary of what impact a global recession will have on the assets they manage.

Mark Silverstein, Chief Investment Officer for Sompo International, is among those attempting to get their arms around how their portfolios will perform in the current environment – and chart a course through uncharted waters.

"We continually assess the risk exposure of our portfolio," says Silverstein. "Over the past few months, we have adapted our analysis to include two additional elements, first and foremost, understanding COVID-19 and its impact on the economy, and second, assessing our portfolio to determine which parts may be impacted by the economic and market forces related to COVID-19."

CIO Randy Brown says Sun Life Financial has done work to create a base case and stressed macro view, then applied that top-down world view onto its portfolio. "At the same time, each analyst is reviewing their exposures from a bottoms-up perspective," he notes. "We are then aggregating the results to estimate the impact to the portfolio. We are reviewing the impacts to credit ratings, capital, and liquidity so we can see how that fits with the broader corporate exposures."

Both CIOs said they found opportunities to take advantage of during market dislocations, which offered something of a silver lining.

"We have taken advantage of the market dislocation to add exposures to high-quality companies at very attractive long-term spreads," says Brown. "We have made private loans and issued commercial mortgages on strong properties and companies with well-structured covenants and collateral. Given our longer-term perspective on our assets, being a liquidity provider in periods of dislocation pays well."

Adds Silverstein, "We always consider opportunities on a risk adjusted basis and, given liquidity conditions over the past month, the best opportunities so far have been in high-quality credit assets and equities. As more time passes, we expect there to be significant corporate stress, which will likely lead to some credit opportunities."

Market volatility driven by the impact of the coronavirus has brought with it more scrutiny by regulators on insurers and financial services companies alike. When asked whether their interactions with regulators had increased in recent weeks, both

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Brown and Silverstein answered in the affirmative.

"We have received and responded to inquiries from a number of regulators who are checking in on the companies they regulate to determine if there should be concerns about asset strength," says Silverstein. "Our investment portfolio performance has weathered this storm well. Our liquidity, capital position and solvency remain very strong and we continue to make decisions that support our goals."

In terms of U.S. GDP for the remainder of the year, Silverstein says, "the near term looks bleak compared to anything we have experienced in our careers. We concur with the view of leading banks about the economic impact for 2020.

"However, effective COVID-19 testing and treatment could lead to a relatively rapid recovery compared to normal recoveries seen in a typical recession," he adds. "Normally, a recovery requires a lot of economic healing. In this case, if the pandemic is tackled, then the economy can pick up where it left off – although the longer the delay, the harder the recovery may be due to the interim damage caused."

Still, all is not gloom and doom – especially from an operational perspective. Both Silverstein and Brown have been pleasantly surprised by their teams' ability to continue to perform efficiently under some unique circumstances.

Operating remotely "has worked quite well, better than I ever could have imagined," Brown says. "We have been fully functional in buying and settling trades, managing portfolios, risk, liquidity, and information flow to the many internal and external interested parties.

"The only issue I have seen is in any person's home bandwidth, given the heavy demand on the 'net as we are all home," he jokes.

At Sompo, "almost immediately, we started daily video team meetings – a combination of catching up on business activities and equally important casual discussion to keep our bonds strong and support each other," Silverstein relates. "Overall, our remote capabilities have enabled us to operate at full strength, with no disruptions to any of our core services, including claims – while keeping our staff safe.

Brown identified some structural changes that might be seen coming, post-pandemic.

"The nature of work could really change off the back of this," he adds. "We have seen that work-from-home works well, so I foresee more agile work environments in the future. Additionally, the role of governments has again changed, and I am not clear how we get that genie back in the bottle. Deficits will be massive, so paying them down will be painful."

"We share the view that it will take time for the global economy to heal and return to robust conditions," adds Silverstein. "I believe that hinges on how persistent COVID-19 is and how effective testing and treatments are.

"Until then, certain industries will be particularly hurt," he says. "In the long run, financial stress in the short term will likely lead to greater dominance by larger companies over their respective industries."

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"Everyone on my team loves the new commute and the 'bring your dog to work' policy," he adds. "That said, this is a stressful time for everyone, both personally and professionally. We are all very grateful that we are healthy and able to work remotely as many others are less fortunate."