PRESCIENT
INVESTMENT MANAGEMENT

THE VIEW FROM CHINA

Liang Du
Chief Executive Officer
Prescient Investment Management China Ltd

At Prescient, we don't usually comment on anything other than quantitative factors, the interpretation of data and what our models are telling us. We believe that investments should be based on research and facts, and that emotions are counterproductive to successful investment decisions.

But in these extraordinary times, we are going to glean insight from a local team working in China, who have witnessed the progression of the COVID-19 virus there first-hand. It may provide valuable perspectives in terms of its outcome, and perhaps offer a different picture to what is currently portrayed in the media.

The outbreak in China started around the end of December 2019 and by the 22nd of January 2020, the Chinese government realised that it was serious – and that containment measures needed to be taken. At that point, confirmed cases in Wuhan were around 400, while in the rest of China, there were another 200 cases. Given the information at hand, the Chinese government decided to place the entire country in lockdown by the 27th of January. Shops and factories closed, mobility was severely limited, and there were almost no people on the streets. By then, cases in Wuhan had risen to over 1 400, with the rest of China reporting 1 400 confirmed cases too.

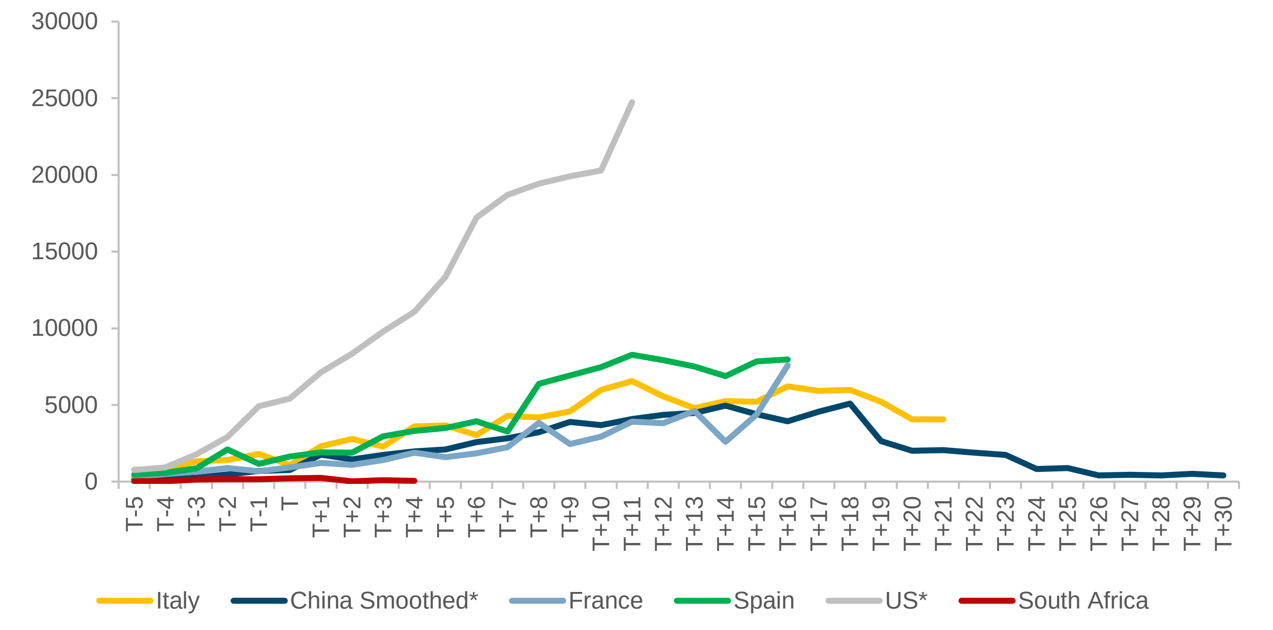
The lockdown had an immediate impact on the transmission of the virus. Social distancing proved extremely effective and with the strict lockdown, new infections and incremental cases were contained very quickly. While infections that occurred prior to the lockdown were worked through the hospital system, new cases peaked around two weeks after the strict lockdown. China phased in resumption to work week by week from the 10th of February.

From the 31st of March, local transmissions all but ended, and life, as well as the economy, went back to almost normal. All Chinese are aware of the dangers of imported cases and strict contact tracing, as well as temperature checks, aim to limit the risks of a secondary outbreak. In the event of another outbreak, authorities will revert to stricter measures. As it stands, the economy is returning to normal, with most restaurants starting to fill up and almost all services restored. The entire process was spread over roughly two months. Although the first two weeks were extreme, with the economy functioning at 0%, work soon resumed in a phased manner within four weeks.

So, what does the Chinese experience offer in terms of possible learnings for the rest of the world?

1. Italy went into a serious lockdown on the 10th of March, with the rest of Europe following suit around 14-15 March.
2. Before the lockdown, there were new infections, and these are currently working their way through the hospital system.
3. We are already seeing the impact of the Italian and European lockdown, and it seems as if new cases in Italy and Spain have peaked.
4. On the whole, Europe started lockdowns later than China and is therefore likely to experience far more cases. Given that viruses spread exponentially, starting lockdowns a week later will imply materially more infections.
5. However, there’s no reason to believe that the European lockdowns would not have any impact.
6. The US is approximately a week behind Europe in terms of action timeframes. Worse yet, the US started their lockdown later than any other country and even as we speak, the lockdown is only on a state-by-state basis.
7. South Africa took decisive action much earlier in terms of action of response timeframes than the US or Europe. As such, if our detection pattern is similar, we should see a much better outcome than the US or Europe. The next 10 days or so will be crucial and initial signs indicate that the South African spread is less severe than Europe or even the rest of China.

Daily New Cases with time T as Lockdown Day



** China’s data was smoothed for a different testing standard in Hubei when testing kits were low. The total number was unaffected. The chest X-ray diagnostic cases were smoothed over the previous week.*

Source: Wind, end March 2020

Global central banks announced large-scale monetary stimulus (Unlimited QE in Europe and US, even direct purchases of investment-grade bonds and ETFs), as well as some of the largest fiscal stimulus in history. The US stimulus is US$ 2 trillion – double the size of the 2008-crisis bailout. China is slow dripping fiscal stimulus news into the market daily, but the overall early analysis seems to indicate a package of around 5-8% of GDP, mostly into infrastructure such as 5G, tourism and high-tech industry – as well as support for small enterprises. No fiscal stimulus will be useful until the virus is under control, hence strict lockdowns become crucial.

Valuations are currently extremely cheap, sentiment negative, and policy extremely supportive. As such, we are keeping a very close eye on our proprietary indicators, and we're ready to increase risk when they show a recovery – either in the real economy or in sentiment.

China started with much cheaper valuations than the rest of the world, combined with being first to emerge from the coronavirus crisis. As was the case during the 2009 recovery, it is the market likely to lead the world towards recovery.

Overall, we are finding some of the best opportunities in almost a decade in the current dislocation. Prescient's process has always been to quantify and take risks when being paid to take them. This is the best time to do so since we started the fund. As a team based in China, we witness the initial reaction from the West, which was a belief that it was a Chinese virus that wouldn't affect them. Italy shattered that illusion and other western countries also soon experienced the same viral spread. Similarly, the current sentiment in the West seems too negative, with people talking about social distancing lasting for more than 18 months.

Although most cities will heighten awareness, the reality of full lockdowns would generally last 3-5 weeks before a material decrease of new virus cases can be expected. With the same virus and similar measures, there's no reason to believe that China's outcome cannot be replicated around the world once appropriate measures are in place. Once the impact of the virus has been contained, 5-10% of GDP stimulus should be more than enough to kickstart the economy. The longer-term impact of global money printing will remain to be seen. The monetisation of fiscal deficits could be the end of low inflation, or modern monetary theory could still prove to be true, yet in either case, real assets would be a better place to be than cash. To the team here in China, it looks like a great opportunity to do research and start increasing risk.

Ends.

About Prescient:

- Prescient Holdings (Pty) Ltd is a diversified, global financial services group with a 21-year track record of providing solutions to our clients in Asset Management, Investment and Platform Administration, Retirement Solutions, Stockbroking and Wealth Management. As at 31 December 2019, the group had R98.4 billion client assets under management (AUM) and administered R478 billion client assets (AUA), split between asset admin (R328 billion) and unit holder admin (R150 billion). Prescient has established operating businesses in three main jurisdictions and has successfully operated for 21 years in South Africa, 12 years in Ireland & the UK and six years in China.

- Prescient Management Company (RF) Pty Ltd (the manager) is approved under the Collective Investment Schemes Control Act (No.45 of 2002). Prescient Investment Management is an authorised Financial Service Provider (FSP 612) under the Financial Advisory and Intermediary Services Act (No.37 of 2002).

PRESCIENT INVESTMENT MANAGEMENT (PTY) LTD

Block B, Silverwood, Silverwood Lane, Steenberg Office Park, Tokai, 7945
P.O. Box 31142, Tokai 7966 Tel: +27-21-700 3600 Website: www.prescient.co.za