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CFA Institute - Insights on how Covid-19 has impacted the Investment Industry

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Why did the CFA Institute release a recent report covering the impact of Covid-19 on financial markets and the investment industry?

Well, as Covid-19 continued into 2021, we felt that there was a lot of noise and interpretational issues in how the crisis is being analysed, particularly its impact on capital markets and asset pricing. So we wanted to leverage on our global and professional membership to provide an honest and unbiased perspective on the most critical issues.

This follows the first Covid-19 survey that we did exactly a year ago. And this time round, globally, we have about 6,000 responses, about 800 of which were from Asia Pacific. And we have collected a lot of very rich and insightful data at many levels. So for example, on the market levels, asset pricing, whether QE (quantitative easing) should stay or whether QE should go, as well as some of the social economic consequences as a result of the monetary stimulus that we've seen. And our goal is really that through the report to surface to policymakers, key insights that we have gleaned from our global member base to better inform policy making going forward.

What were some the key highlights from the report?

Some of the most interesting takeaways from the reports were asset pricing, whether governments should exit the markets, as well as the social-economic consequences of some of these economic and monetary stimulus.

So on asset pricing, last year there was an overwhelming majority of respondents that told us the crisis increased the chance of asset mispricing. Actually, the number was as high as 96% last year. And that was due to a combination of liquidity dislocations and public authorities' intervention. And this year, what our membership has been telling us is that there is still doubt that asset pricing has returned to normal. And

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55% of respondents in APAC are telling us that they thought global developed market equities were basically out of sync with the underlying economies, that they recovered too quickly, and are due for correction in the next one to three years. And only 3% of APAC respondents thought that equity markets were properly priced.

And if we look at the Buffett Indicator, which tracks the ratio of stock market capitalisation to GDP, it was at an all-time high in the third quarter of 2020. So the temptation is to keep dancing while the music is playing.

Now, so the next question becomes should QE stay or should QE go? What's the timing for governments' exit? And this is a very divisive issue. And I think if we have any takeaways from the report, it is that our membership is quite split on the issue. Last year, when we asked this question, the split was exactly 50/50. This year we're seeing a slight shift. So globally, 51% of respondents said, it is important to get back on a normal course as soon as possible, versus 43% saying that it's important to continue to support people, businesses and the economy.

But interestingly for Asia Pacific, the regional view in Asia Pacific is different from the global dataset. In fact, it's flipped around. In Asia Pacific 51% of respondents indicated a preference to sustained action over getting on a normal footing, which was 44%. And the markets in Asia Pacific that are most strongly supportive for continued easing include Japan, Singapore, India, and Pakistan, and those that are most supportive for exit were Australia and China.

And I think it's an important question, it's also very divisive, as I said. I think the relationship between monetary supply and inflation and economic growth and productivity is very complex, but I think the question has to be asked as to whether QE will continue to be effective if it goes on indefinitely. Like all things there is a law, called the law of diminishing marginal utility, and I don't think QE is immune.

Are there any particular take-aways that affect clients in Asia?

One of the questions that we asked our respondents was 'which asset classes would be most impacted if money becomes tighter', i.e., if there was a tighter monetary policy and if interest rates started going up. The top three asset classes that would be most negatively impacted, according to our respondents were number one, growth stocks, number two, high yield corporate bonds, and for Asia Pacific respondents, number three, emerging market stocks.

Now it doesn't mean that there are no opportunities. The top three asset classes that would most benefit are value stocks, the dollar index and gold. So it's a mirror image there. I think for Asia Pacific respondents, they are particularly concerned about emerging market bonds and stocks, which is understandable because a large part of Asia Pacific markets are still developing. And if you look at these results and couple that with the overall sentiment or overall belief that equity markets recovered too quickly, and that they're due for correction, and that they're out of sync with underlying economic fundamentals, then I think, as investors, we have to really look carefully at our portfolios and decide what sorts of risks we would like to take on. ■