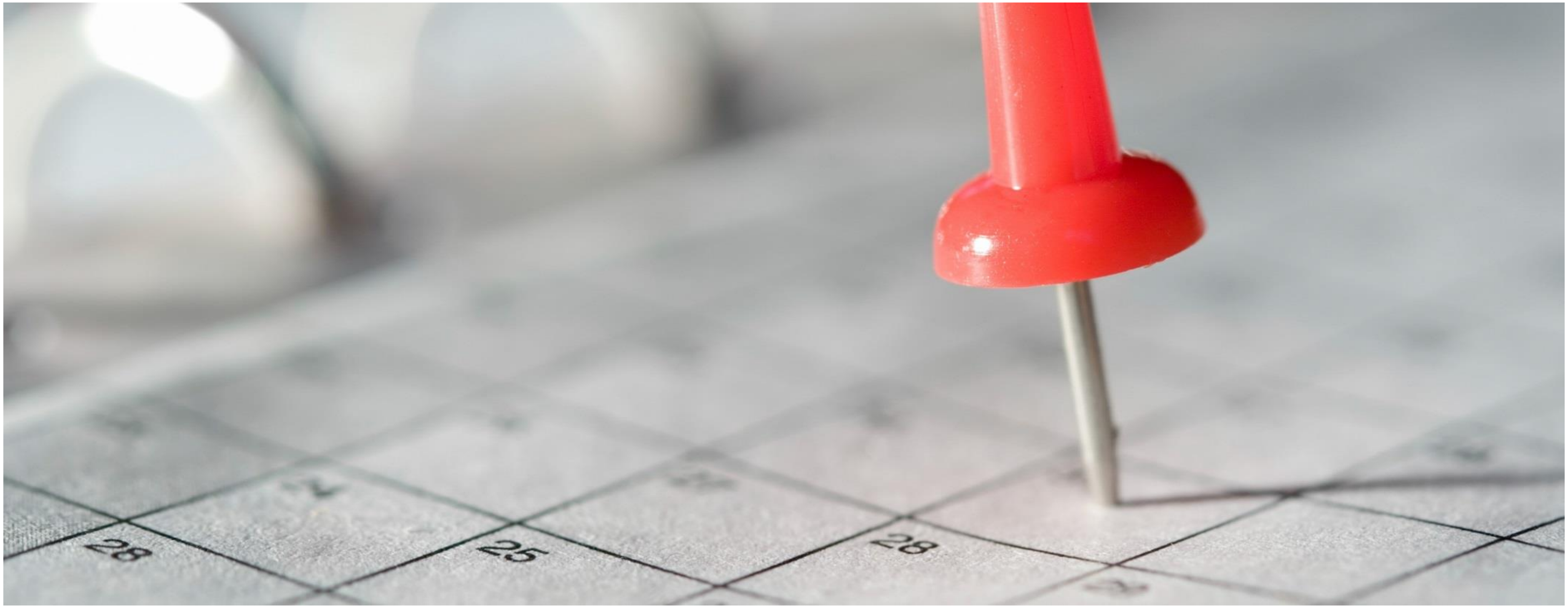


Market Update – COVID-19

May 12, 2020 Close unless otherwise stated

QAS Institute and Faculty of Actuaries® Quality Assurance Scheme

Aon Empower Results®

Prepared by Aon

Our Views

- Markets have bounced back sharply, boosted by signs of a “flatter” virus trajectory across major developed economies and global governments and central banks being willing to take extraordinary measures to support economies.
- Sustainable gains from here on look much more difficult with valuations now looking stretched and the economic consequence of the pandemic lockdown still uncertain.
- Bond yields remain at rock bottom levels, as global QE programmes and policy interest rates hold yield curves down. This is unlikely to change over the medium-term.

Actions for client portfolios

- **Our recommendation on buying equities to rebalance allocations have changed to a “no action” policy.** This does not imply an expectation that large market falls are necessarily imminent. It is more that at this stage, market levels and valuations suggest inferior rewards for taking on more equity risk.
- **Some reallocation towards building credit positions which have drifted underweight following recent market declines remain appropriate**. The scale of the market rebound has not had quite the same impact on investment grade credit markets (even though high yield bonds have moved into much less attractive territory).
- **Diversification has paid off in these difficult market conditions, and we believe they retain an important role in portfolios given the degree of market uncertainty.** Further market weakness will improve the case for using diversifiers as a funding source for adding risk to portfolios.
- **Duration positions should be taken with care.** A mild underweight looks reasonable, but we do not believe it is likely that yields will move up very much even after the virus scare has passed. Hedge ratios should be managed accordingly.

What we are watching:

- Signposts for the duration of global economic weakness. We continue to expect a relatively low octane economic recovery when lockdown restrictions are lifted. More confidence here would help the case for adding risk to portfolios.
- The scale of valuation adjustments in equities and credit, alongside technical and sentiment indicators pointing to a more sustainable market recovery.

COVID-19 Update

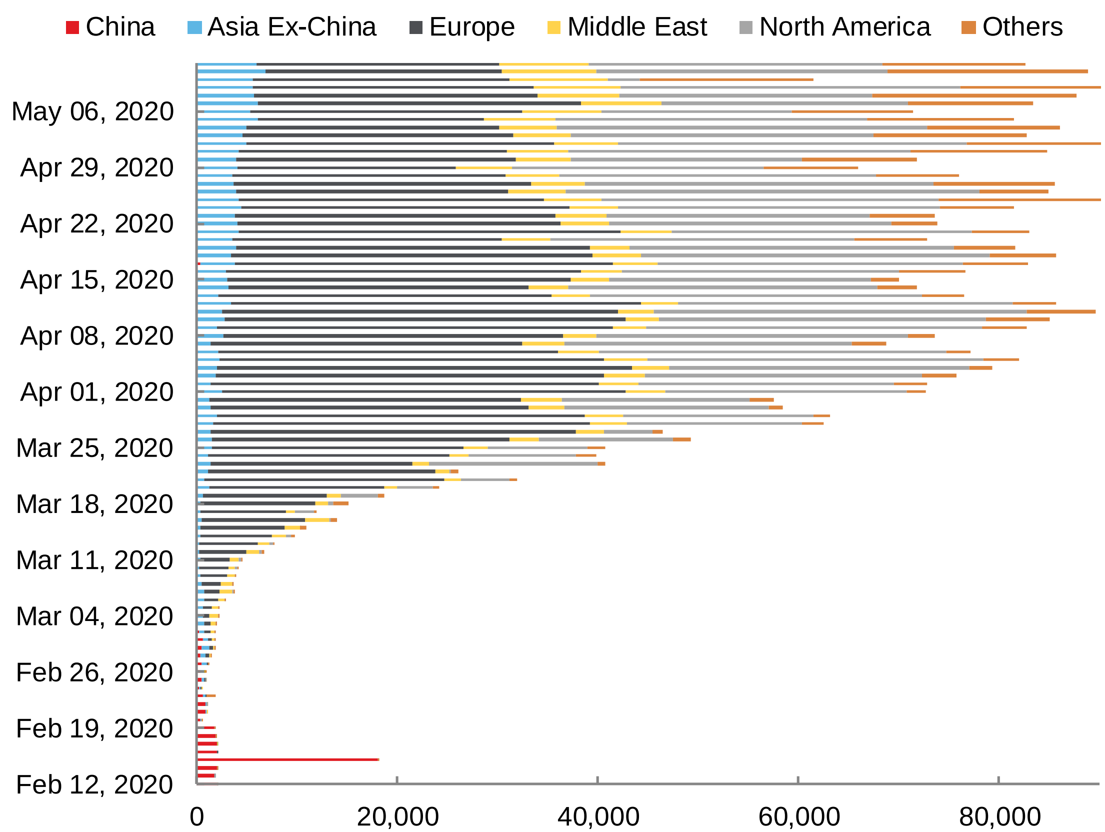
Current Situation (12 May 2020)

Global	
Confirmed Cases	4,088,848
Deaths	283,153

Europe	
Confirmed Cases	1,755,790
Deaths	157,880

United States	
Confirmed Cases	1,298,287
Deaths	78,652

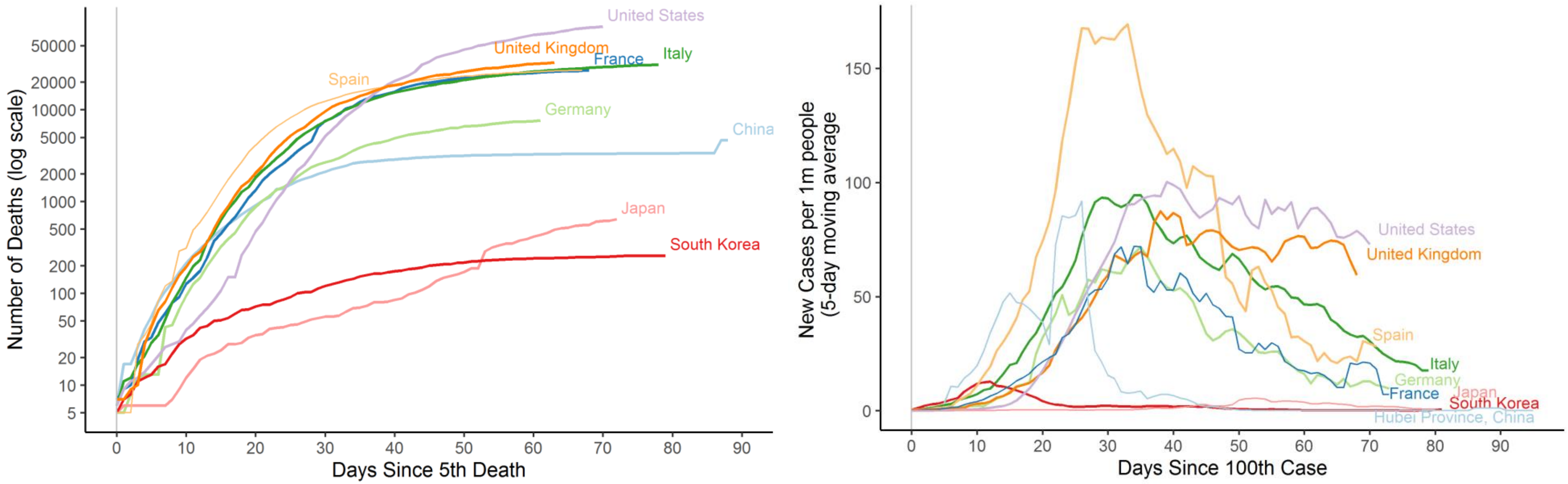
New COVID-19 Cases



Source: FactSet, World Health Organization, National Health Authorities. Regions not shown above, along with countries where there is not a significant COVID-19 outbreak has been categorized under “Other”. .

COVID-19 Virus Trajectory

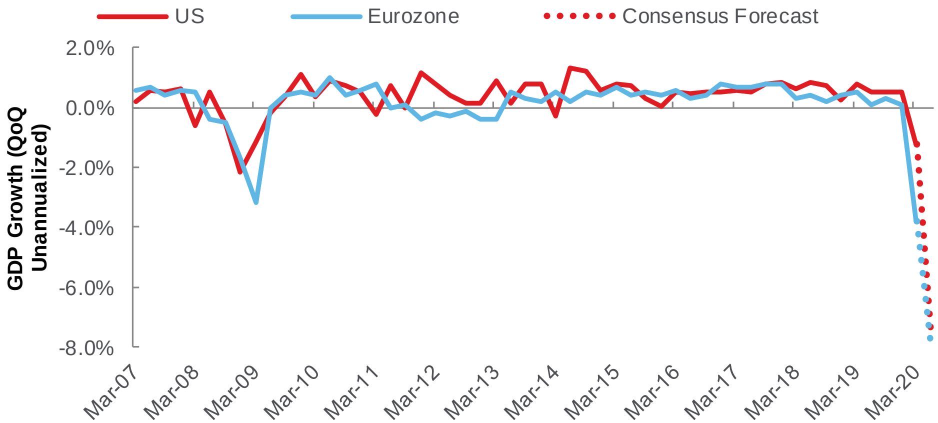
- The trajectory of the outbreak will be key in determining how long containment policies remain in place and how the economy fares.
- The virus appeared to have peaked in Europe and the US after lockdown measures were implemented. However, a “second wave” outbreak remains a risk if these measures are lifted.



Source: Aon, European Centre for Disease Prevention and Control, Hubei Province data sourced from John Hopkins University.
Data as at 12 May 2020.

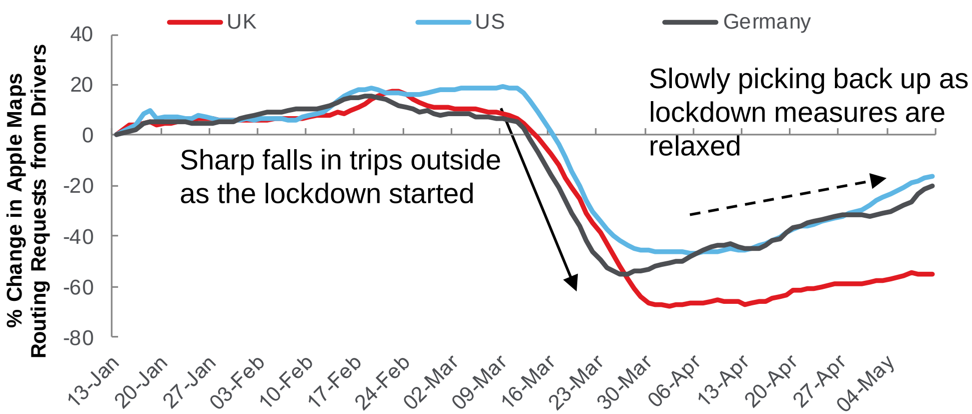
An Economic Catastrophe

Q1 GDP figures are indicating a sharp economic contraction, with worse expected in Q2



Source: Bloomberg

Apple Maps data point to some improvement in transport activity, but activity remains substantially below normal

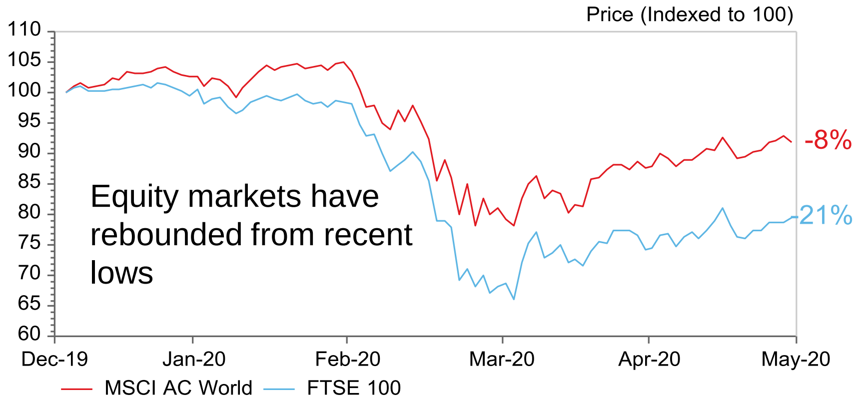


Source: Apple. 7-day moving average shown.

- The “Great Lockdown” looked to have been effective so far in containing the spread of COVID-19, but at the expense of what’s likely to be the worst recession in generations
- The scale of the economic damage is starting to become apparent
  - c.22% of the US working population have filed for unemployment benefits since mid-March
  - Eurozone GDP growth in Q1 was the worst on record, with France recording its worst growth figure since 1945
- The length and severity of the recession will depend on how quickly things can get back to normal
  - Germany, parts of the US, and a few other countries have started to relax some of their lockdown measures
  - Getting back to normal would likely take a long time. Non-essential trips may continue to be avoided even if official lockdown measures ended
  - A severe “second wave” outbreak is a risk, and if the virus starts escalating again another lockdown may be needed

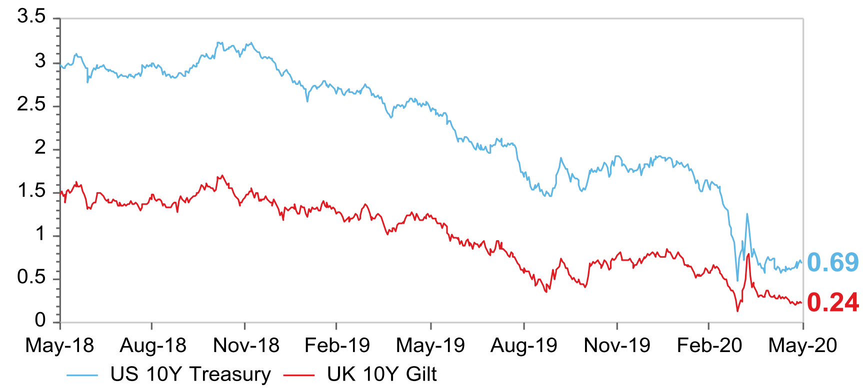
Market Reactions

Equity Market YTD (GBP terms)



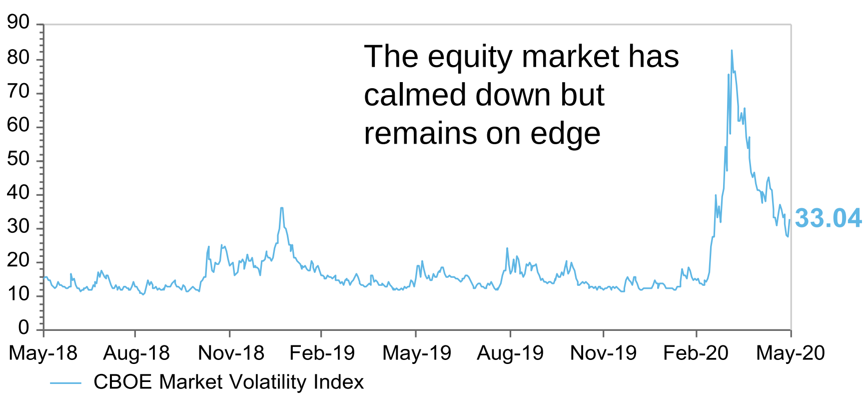
Source: FactSet

Government Bond Yields (%)



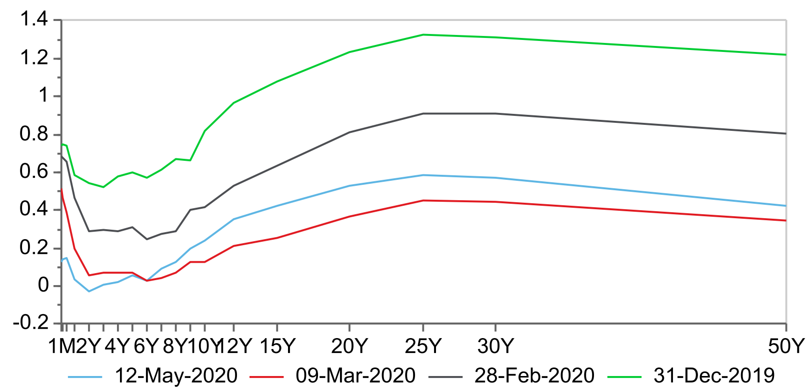
Source: FactSet

VIX



Source: FactSet

UK Gilt Yield Curve

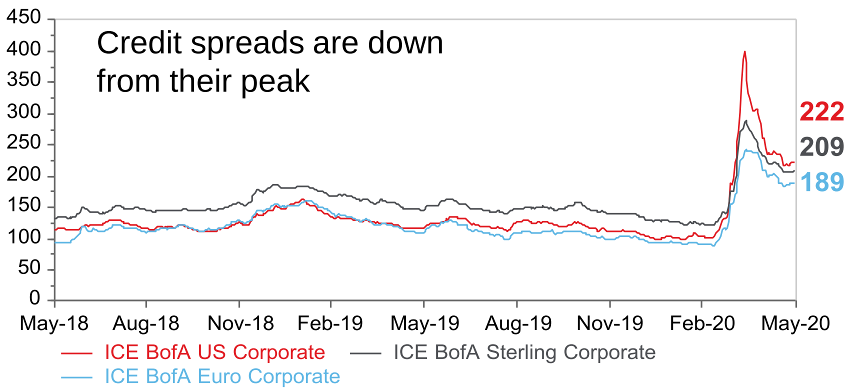


Source: FactSet

Past performance is no guarantee of future results.

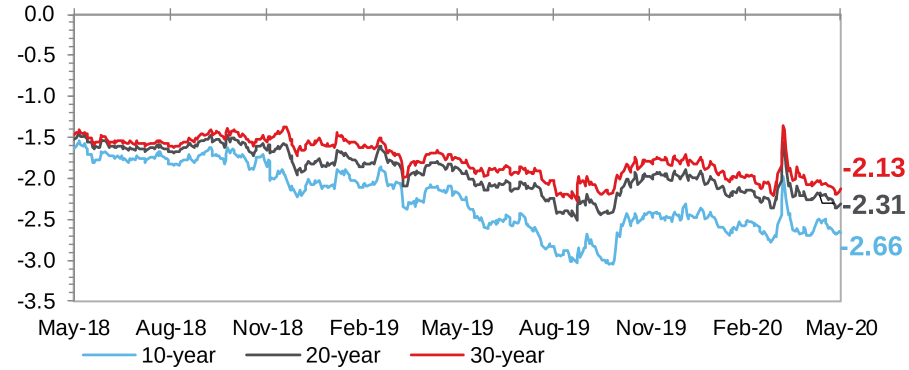
Market Reactions

Investment Grade Credit Spreads (bps)



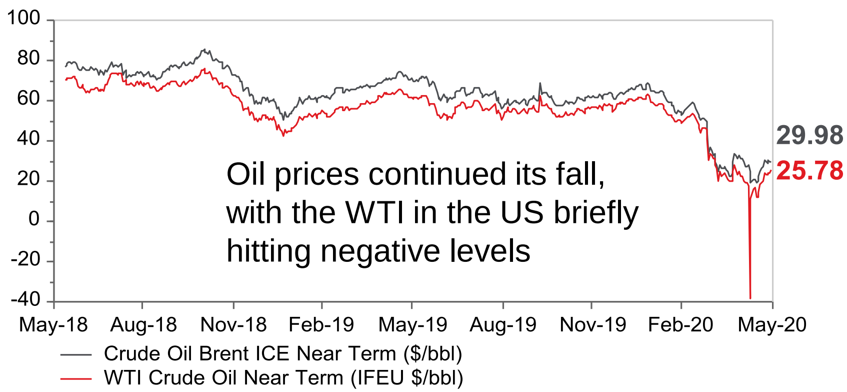
Source: Factset

Real Yields (%)



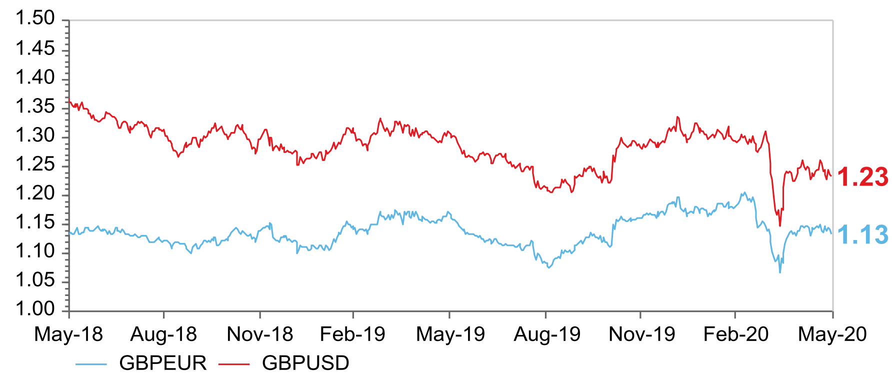
Source: Bloomberg

Crude Oil Spot Price



Source: FactSet

Sterling has fallen sharply but has recovered some of its losses

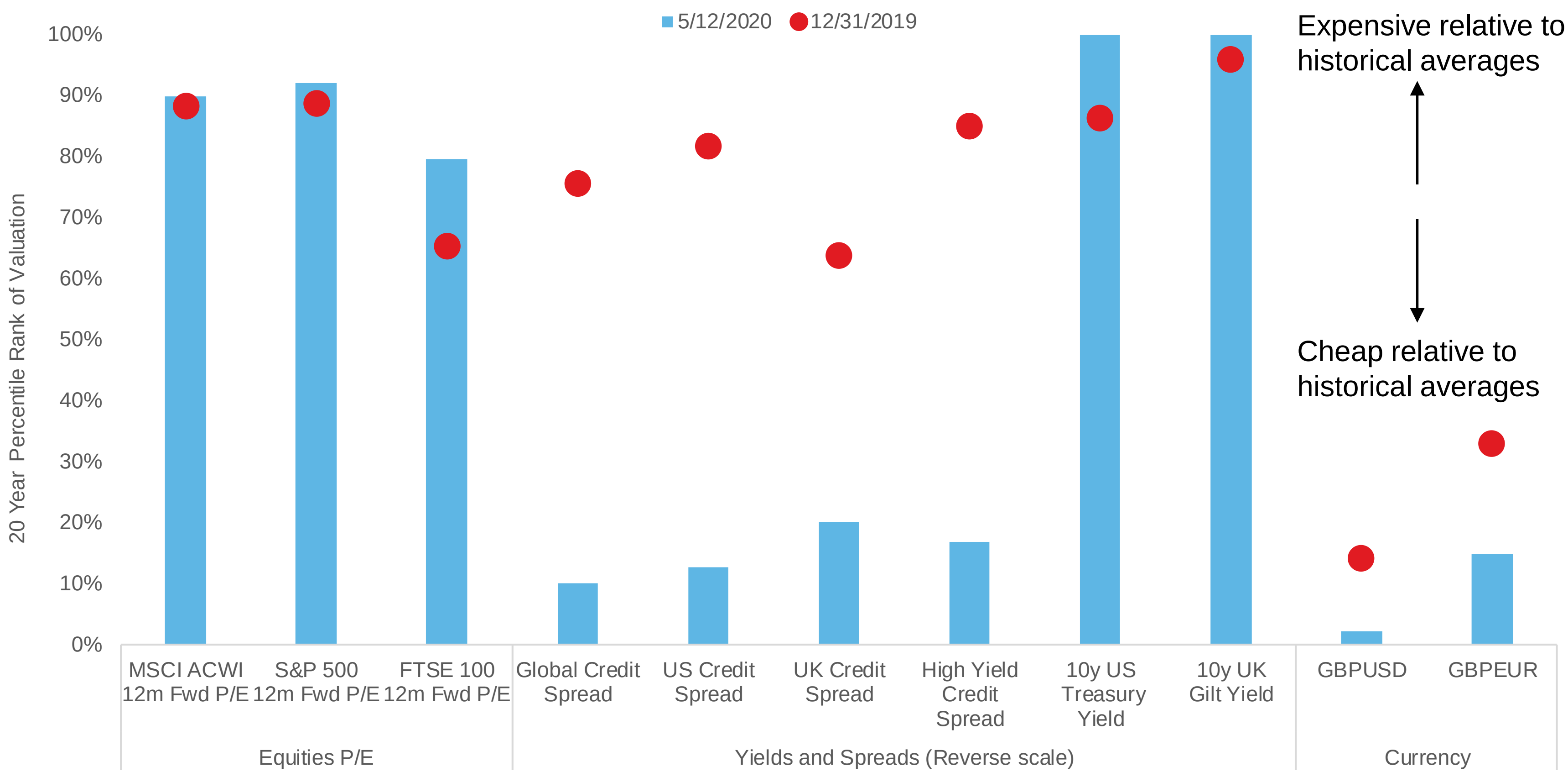


Source: FactSet

Past performance is no guarantee of future results.

Market Valuations

Markets have re-rated extremely fast, but there is some uncertainty around how much value there is. Forward looking measures of value may be using stale estimates, as the economic impact is so uncertain.

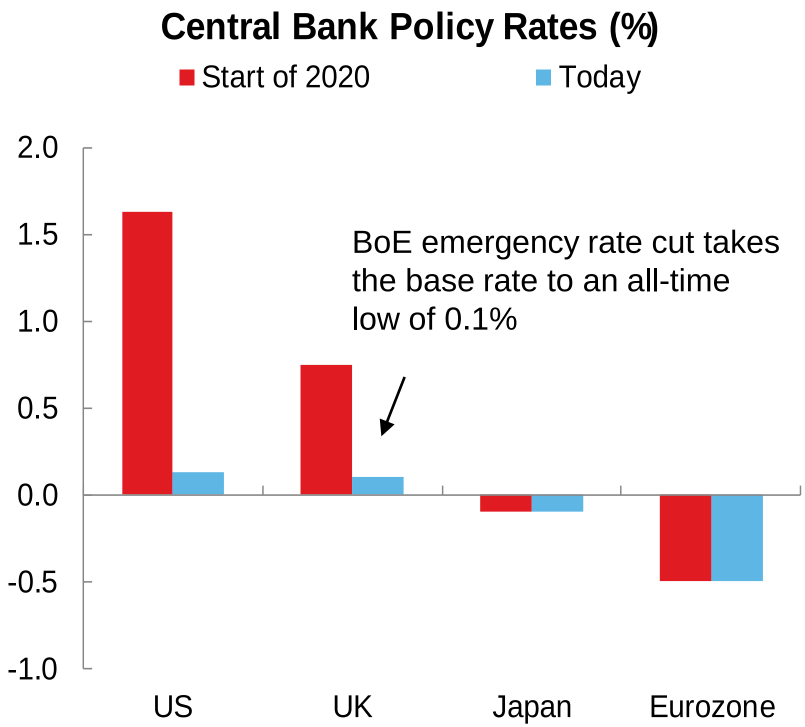


Source: Aon, Factset

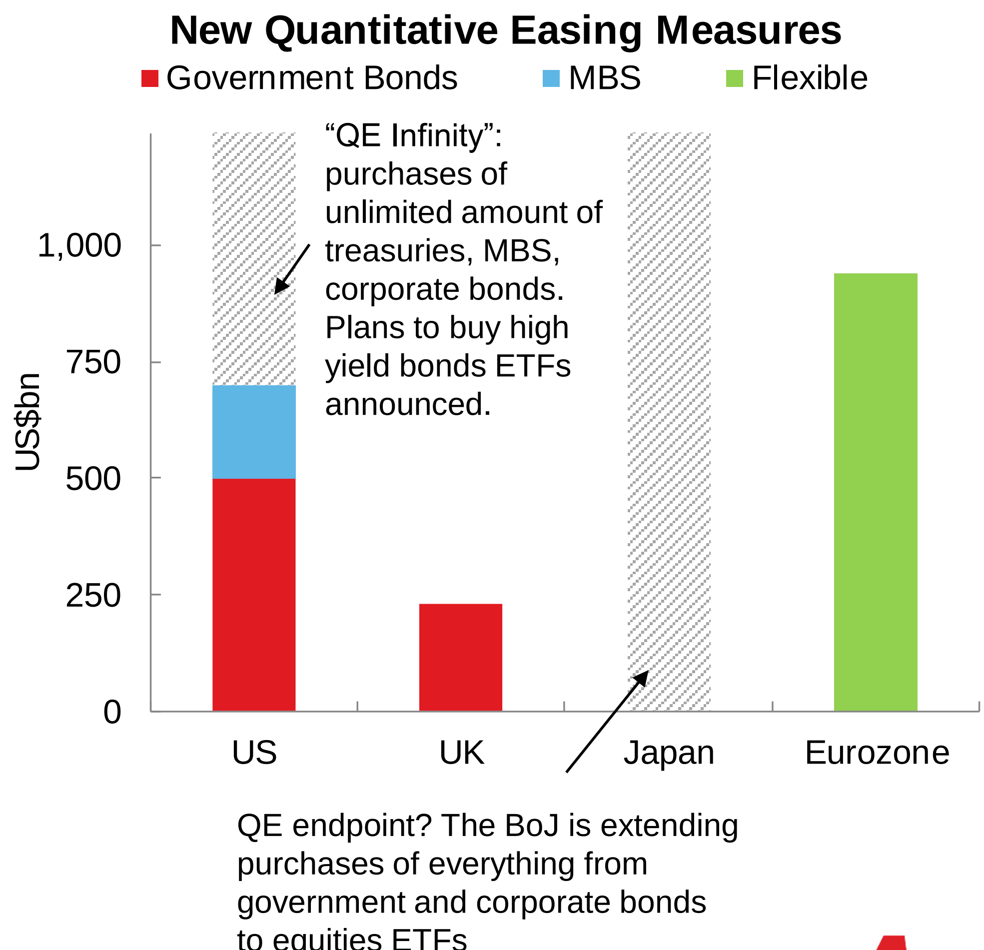
Notes: Valuations used: Equity markets = Next Twelve Month PE Ratio, Credit Spread = Option Adjusted Spread, Treasury Yield = Yield To Maturity

Central Bank Actions

- Where possible central banks around the world have eased policy, but with rates being low there is a limit.
- Unprecedented new quantitative easing measures have been announced to provide further monetary stimulus.



Source: Aon, Bloomberg OIS Pricing
Past performance is no guarantee of future results.



Announced Fiscal Packages

USA	▪ Congress has passed a c.$2 trillion fiscal stimulus package. The package expands jobless benefits and provides direct transfers of up to $1,200 for Americans earning less than $75,000 per year ▪ State of Emergency declared releasing $50bn to States to deal with virus ▪ April tax date to be delayed, providing a $200-300bn bridge loan to households
UK	▪ £330bn in loans and £20bn in other aids have been announced to provide help to businesses. ▪ The government has agreed to cover 80% of salary for employees who are unable to work due to coronavirus related shutdowns. Similar schemes have also been introduced for self-employed individuals.
Japan	▪ Japan has approved a c.$1 trillion fiscal stimulus package. ▪ A variety of small fiscal measures have also been passed. Two small business loan bills totaling $20bn. $4bn for mask production and stopping viral spread.
Eurozone	▪ The European Union has agreed a €500bn rescue package for countries affected by the pandemic ▪ Germany have launched a €156bn supplementary budget and have launched a loan guarantee program worth up to €950bn (c.28% of its GDP). ▪ France has announced emergency fiscal spending of up to €110bn.

Appendix

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