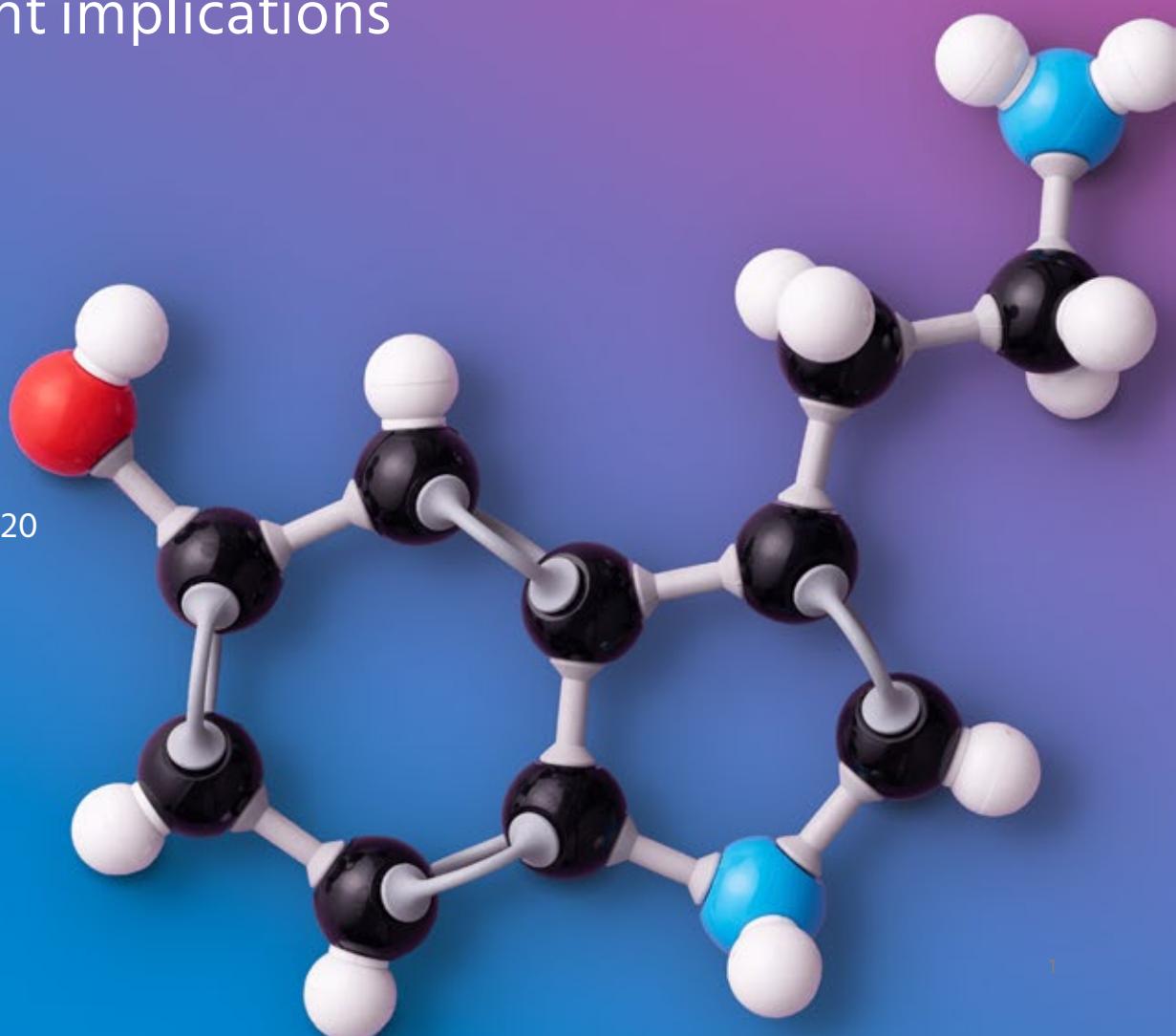


Coronavirus outbreak update

Investment implications

February 28th, 2020



Recent developments and market impact

Toward the end of February 2020, equities and other risk assets sold off, and safe-haven assets rallied amid increasing concerns about the novel coronavirus. The virus, now known as SARS-CoV-2, is expected to spread further than was initially anticipated. Over the three trading sessions from February 21 through February 25, global equity markets fell by around 6% while gold increased by over 2%.¹ The US 10-year Treasury yield edged closer to the 1.3% mark, the lowest level ever recorded.

The number of cases across the globe has now increased to 80,239, as of February 25, according to the World Health Organization (WHO).² Meanwhile, WHO has also reported 2,700 deaths from COVID-19 (the disease associated with SARS-CoV-2). The vast majority of these cases remain within the Hubei province in China, which is the epicenter of the outbreak. Outside China, there have been 2,459 cases and 34 deaths reported in 33 countries. With sadness, we note that more people have now died from COVID-19 than died during the SARS outbreaks between 2002 and 2004.

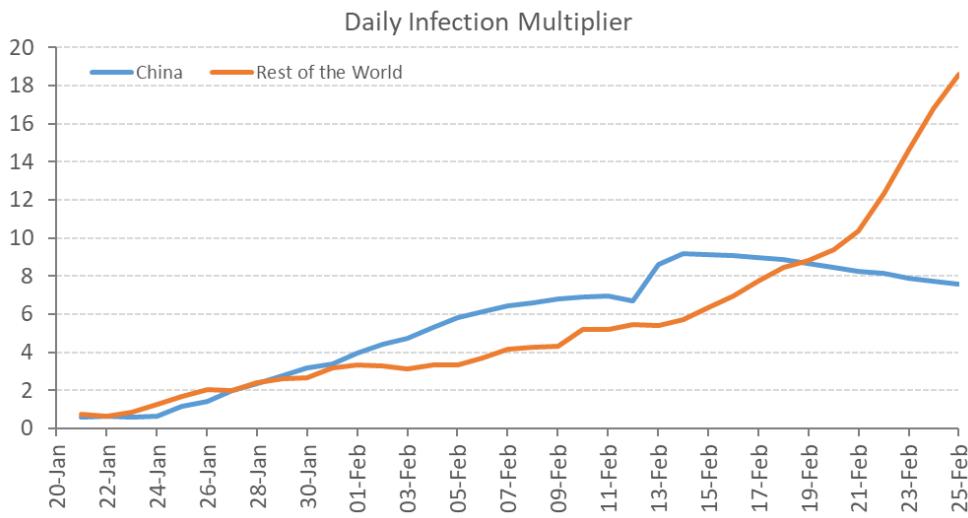
Outbreaks outside China

Although the number of cases outside China is low, there is concern about the rapid escalation in other countries. As the charts below show, the infection multiplier (a measure of the speed of the infection spread) and new cases outside China have increased significantly over the last week. Over the week up to February 25, the number of cases in Korea rose sharply from 30 to 977, while in Japan cases jumped from 59 to 157 (excluding the cruise ship Diamond Princess). In Italy, the number of cases rose from 3 to 229.³ In both Korea and Italy, where numbers have risen most dramatically, outbreaks were concentrated in specific areas.

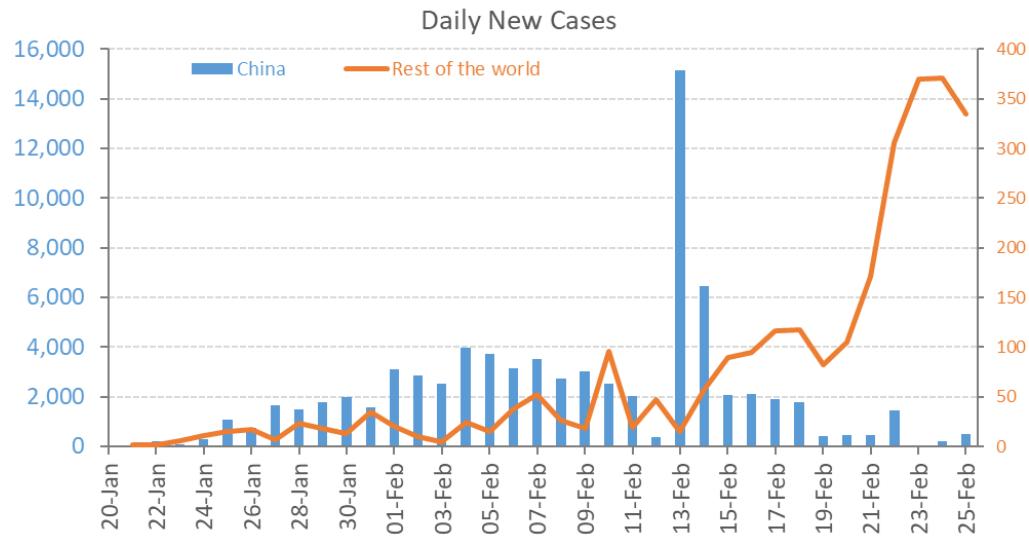
¹ For more information on gold, please refer to our latest paper "[Gold – You're Indestructible](https://www.mercer.com/our-thinking/wealth/gold-you-are-indestructible.html)," available at <https://www.mercer.com/our-thinking/wealth/gold-you-are-indestructible.html>

² [World Health Organization. Coronavirus Disease 2019 \(COVID-19\) Situation Report – 36, 25 February 2020, available at \[https://www.who.int/docs/default-source/coronavirus/situation-reports/20200225-sitrep-36-covid-19.pdf?sfvrsn=2791b4e0_2\]\(https://www.who.int/docs/default-source/coronavirus/situation-reports/20200225-sitrep-36-covid-19.pdf?sfvrsn=2791b4e0_2\).](https://www.who.int/docs/default-source/coronavirus/situation-reports/20200225-sitrep-36-covid-19.pdf?sfvrsn=2791b4e0_2)

³ [World Health Organization. Coronavirus Disease 2019 \(COVID-19\) Situation Report – 28, 17 February 2020, available at \[https://www.who.int/docs/default-source/coronavirus/situation-reports/20200217-sitrep-28-covid-19.pdf?sfvrsn=a19cf2ad_2\]\(https://www.who.int/docs/default-source/coronavirus/situation-reports/20200217-sitrep-28-covid-19.pdf?sfvrsn=a19cf2ad_2\) \(using February 17 as base\).](https://www.who.int/docs/default-source/coronavirus/situation-reports/20200217-sitrep-28-covid-19.pdf?sfvrsn=a19cf2ad_2)



Source: Kompa, Mercer. The daily infection multiplier is defined as the ratio of total cases to date compared with the number when the outbreak was first reported (January 20, 2020), adjusted for the number of days since the outbreak.



Source: Kompa, Mercer.

Quarantine measures have been taken in the two affected regions in Italy, similar to those taken in the Hubei province. The small towns that seemed to be the main sites of the Italian outbreaks have been locked down by the military. In Korea, the outbreak appears to have emerged from a mega-church and the affected city has put voluntary quarantine measures in place. Italy, Japan and Korea are all key manufacturing hubs and parts of the global supply chain, contributing 1.7%, 4.0% and 1.6%, respectively, to estimated global GDP, according to the International Monetary Fund.⁴ Our main concern is that the virus may spread rapidly and untraceably into other countries, disrupting economic activity in much the same way as it has in China, but on a global basis. In Italy, authorities have struggled to trace the origin of the outbreak, leading to the concern that a hyper-contagious individual (a so-called “super-spreader”) is still causing infections. Furthermore, the outbreaks in Italy and Korea have occurred in important manufacturing heartlands that are key drivers of economic growth for those countries.

There is also unease about the current outbreak in Iran, the scale of which has likely been hidden for weeks. The potential lack of cooperation and transparency from Iran increases the risk of the virus spreading across the Middle East, especially due to pilgrimage flows.

As a result, future disruptions to regions of similar economic importance are a plausible scenario, and there could well be random economic shocks to the global economy. In such cases, we expect heavy-handed measures such as lockdowns and travel restrictions, even if they come at a high economic cost; the political cost of inaction would be far too high for most governments to contemplate. Although good progress has been made on treatments, including a vaccination, large-scale manufacture and distribution are likely to take months.

Meanwhile in China, the number of reported new cases continues to trend downward, aside from a spike on February 13, due to a change in the classification method.⁵ Further quarantines, delays to resumption of economic activity and restrictions on people movements appear to have contributed to slowing the spread of the virus outside the Hubei province. Chinese authorities reported just nine new cases in other provinces on February 25.

Economic impact

Aside from the concern regarding the spread of SARS-CoV-2 beyond China, the extent to which economic activity is being disrupted within China appears to be greater than many economists and market participants had previously thought. This has prompted further downgrades in economic forecasts for the first quarter and calendar year 2020, both in China and across the globe.

⁴ IMF October 2019 World Economic Outlook database

⁵ [World Health Organization. Coronavirus Disease 2019 \(COVID-19\) Situation Report – 24, 13 February 2020, available at https://www.who.int/docs/default-source/coronavirus/situation-reports/20200213-sitrep-24-covid-19.pdf?sfvrsn=9a7406a4_4](https://www.who.int/docs/default-source/coronavirus/situation-reports/20200213-sitrep-24-covid-19.pdf?sfvrsn=9a7406a4_4)

For example, consensus forecasts for first-quarter Chinese GDP growth have gone from 6% to heavily negative. With China now representing almost 20% of the global economy, this will have a material impact on global growth for the quarter and will be made worse by the spillover impacts on other economies.

Equity markets have also revised their earnings expectations modestly downward, with the MSCI Emerging Markets Index implied earnings per share for the next year falling approximately 2% over the past month. Although this is only a slight fall, it does follow a contraction in earnings in 2019 on the back of trade tensions and slowing global growth.

So far, no major economic data highlighting the extent of disruptions have been released (the January quarantines and shutdowns coincided with the regular Chinese New Year holidays). The first February data to be released will be the Purchasing Manager Indices, expected between February 26 and March 2. According to Bloomberg, economists are currently forecasting the official and unofficial (Caixin) manufacturing PMIs for China to fall significantly. This is not surprising given that surveys point to only half of firms having resumed activity after the Chinese New Year, and those are operating at lower capacity due to restrictions on workers. A number of proxy indicators such as traffic congestion, coal consumption and subway rides all point to a very slow resumption in activity.

Beyond China, there is mounting evidence of COVID-19 causing a degree of economic disruption. Factories have been forced to reduce capacity and send workers on unpaid leave due to inputs from China not being delivered. Earlier in February, Apple indicated that it might not meet its quarterly target as a consequence of disrupted production and stores' closure in China. Countries reliant on spending from Chinese tourists, including the US, are also feeling the pinch. Conferences and events across the world have been canceled or postponed. If the virus spreads more widely, we expect these disruptions to become more systematic.

Outlook

The recent outbreaks of the virus will only add to the uncertainty and significantly widen the range of outcomes for global economic growth.

If the downward trend of new cases in China continues, Chinese authorities may loosen restrictions on business in those provinces deemed less at risk of spread of COVID-19, enabling economic activity to resume. Economic data is likely to be very soft in February, however it may stabilize in March before ultimately returning to normal in April. In such a scenario, we still expect a v-shaped recovery in activity, but the inflection point may be later than we previously anticipated.

Manufacturing activity that did not take place in February or early March could be made up in subsequent periods. But some services activity are unlikely to be recovered, such as those related

to the cancelled Lunar New Year celebrations. As a result, full-year economic growth figures for China are likely to be lower than expected, weighing on corporate earnings.

As for the rest of the world, much depends on whether the recent outbreaks outside China will be contained, how long this will take, and whether we will see many more outbreaks causing further disruptions, which is now highly likely. Countries reliant on tourism could well see lower growth for the year: The high-profile case of the cruise ship forced to weigh anchor off the coast of Japan might put off travelers all over the world from planning vacations until the epidemic is completely over. However, in some countries, fiscal easing is likely to bring some spending forward and thus smooth the growth impact. Moreover, central banks could employ another round of monetary stimulus.

In summary, although our base scenario is slightly impaired, we expect positive global growth for 2020, with the second half of the year recovering a substantial amount of the growth lost in the first half. That said, we caution that there is material uncertainty around our base scenario, and the situation could take a dramatic turn for the worse, should this become a prolonged global pandemic with many lockdowns and quarantines emerging across the world.

Dynamic asset allocation (DAA) view

Overall, our base case remains intact – we still expect global economic growth to return to trend over 2020 and 2021, albeit with higher downside risks than previously anticipated.

From an asset allocation perspective, we continue to recommend a neutral allocation to listed equities. Equities could fall further if COVID-19 becomes a global pandemic and efforts to control the spread further disrupt economic activity. However, equity market investors should look beyond short-term economic disruptions, and the downside could be cushioned by any monetary policy response.

We maintain our slight preference for emerging markets over developed markets. Emerging markets continue to be attractively valued on balance and likely to benefit from loose financial conditions. For the time being, volatility is likely to persist.

Important notices

References to Mercer shall be construed to include Mercer LLC and/or its associated companies.

© 2020 Mercer LLC. All rights reserved.

This contains confidential and proprietary information of Mercer and is intended for the exclusive use of the parties to whom it was provided by Mercer. Its content may not be modified, sold or otherwise provided, in whole or in part, to any other person or entity without Mercer's prior written permission.

Mercer does not provide tax or legal advice. You should contact your tax advisor, accountant and/or attorney before making any decisions with tax or legal implications.

This does not constitute an offer to purchase or sell any securities.

The findings, ratings and/or opinions expressed herein are the intellectual property of Mercer and are subject to change without notice. They are not intended to convey any guarantees as to the future performance of the investment products, asset classes or capital markets discussed.

For Mercer's conflict of interest disclosures, contact your Mercer representative or see <http://www.mercer.com/conflictsofinterest>.

This does not contain investment advice relating to your particular circumstances. No investment decision should be made based on this information without first obtaining appropriate professional advice and considering your circumstances. Mercer provides recommendations based on the particular client's circumstances, investment objectives and needs. As such, investment results will vary and actual results may differ materially.

Past performance is no guarantee of future results. The value of investments can go down as well as up, and you may not get back the amount you have invested. Investments denominated in a foreign currency will fluctuate with the value of the currency. Certain investments, such as securities issued by small capitalization, foreign and emerging market issuers, real property and illiquid, leveraged or high-yield funds, carry additional risks that should be considered before choosing an investment manager or making an investment decision.

Information contained herein may have been obtained from a range of third-party sources. Although the information is believed to be reliable, Mercer has not sought to verify it independently. As such, Mercer makes no representations or warranties as to the accuracy of the information presented and takes no responsibility or liability (including for indirect, consequential

or incidental damages) for any error, omission or inaccuracy in the data supplied by any third party.

Not all services mentioned are available in all jurisdictions. Please contact your Mercer representative for more information.

Certain regulated services in Europe are provided by Mercer Global Investments Europe Limited, Mercer (Ireland) Limited and Mercer Limited. Mercer Global Investments Europe Limited and Mercer (Ireland) Limited are regulated by the Central Bank of Ireland. Mercer Limited is authorized and regulated by the Financial Conduct Authority. Registered in England and Wales No. 984275. Registered Office: 1 Tower Place West, Tower Place, London EC3R 5BU.

Investment management and advisory services for US clients are provided by Mercer Investments LLC (Mercer Investments). In November 2018, Mercer Investments acquired Summit Strategies Group, Inc. ("Summit"), and effective March 29, 2019, Mercer Investment Consulting LLC ("MIC"), Pavilion Advisory Group, Inc. ("PAG"), and Pavilion Alternatives Group LLC ("PALTS") combined with Mercer Investments. Certain historical information contained herein may reflect the experiences of MIC, PAG, PALTS or Summit operating as separate entities. Mercer Investments is a federally registered investment adviser under the Investment Advisers Act of 1940, as amended. Registration as an investment adviser does not imply a certain level of skill or training. The oral and written communications of an adviser provide you with information about which you determine to hire or retain an adviser. Mercer Investments' Form ADV Parts 2A and 2B can be obtained by written request directed to: Compliance Department, Mercer Investments, 99 High Street, Boston, MA 02110.

Services to be provided by Mercer Investments LLC, which is one of several, associated legal entities that provide investments services to clients as part of a global investment advisory and investment management business (collectively referred to as "Mercer"). Mercer Investments LLC is registered to do business as "Mercer Investment Advisers LLC" in the following states: Arizona, California, Florida, Illinois, Kentucky, New Jersey, North Carolina, Oklahoma, Pennsylvania, Texas, and West Virginia; as "Mercer Investments LLC (Delaware)" in Georgia; as "Mercer Investments LLC of Delaware" in Louisiana; and "Mercer Investments LLC, a limited liability company of Delaware" in Oregon.

At Mercer, we believe in building brighter futures.

About Mercer

Together, we're redefining the world of work, reshaping retirement and investment outcomes, and unlocking real health and well-being. We do this by meeting the needs of today and tomorrow. By understanding the data and applying it with a human touch. And by turning ideas into action to spark positive change.

For more than 70 years, we've been providing trusted advice and solutions to build healthier and more sustainable futures for our clients, colleagues and communities.

Welcome to a world where economics and empathy make a difference in people's lives.

Welcome to brighter.

For further information, please visit
www.mercer.ca

Join the conversation

 [@MercerCanada](#)

 [in Mercer Canada](#)



Important notices

References to Mercer shall be construed to include Mercer LLC and/or its associated companies.

©2020 Mercer (Canada) Limited. All rights reserved

This contains confidential and proprietary information of Mercer and is intended for the exclusive use of the parties to whom it was provided by Mercer. Its content may not be modified, sold or otherwise provided, in whole or in part, to any other person or entity without Mercer's prior written permission.

Mercer does not provide tax or legal advice. You should contact your tax advisor, accountant and/or attorney before making any decisions with tax or legal implications. This does not constitute an offer to purchase or sell any securities. The findings, ratings and/or opinions expressed herein are the intellectual property of Mercer and are subject to change without notice. They are not intended to convey any guarantees as to the future performance of the investment products, asset classes or capital markets discussed.

For Mercer's conflict of interest disclosures, contact your Mercer representative or see www.mercer.com/conflictsofinterest.

This does not contain investment advice relating to your particular circumstances. No investment decision should be made based on this information without first obtaining appropriate professional advice and considering your circumstances.

Information contained herein may have been obtained from a range of third party sources. While the information is believed to be reliable, Mercer has not sought to verify it independently.

How We Can Help

Investments and retirement require sophisticated solutions. We understand that providing long-term financial wellness solutions leads to better returns. We offer research and advice on how to assess risk and design benefits programs while keeping in mind the need to optimize throughout changing times. With in-depth knowledge of the complexities and ever-changing factors that impact investments, Mercer's consultants help you make effective decisions that align with your business needs and ensure more rewarding futures for your employees.

As such, Mercer makes no representations or warranties as to the accuracy of the information presented and takes no responsibility or liability (including for indirect, consequential, or incidental damages) for any error, omission or inaccuracy in the data supplied by any third party.

Pension & Investments rankings are based on survey responses from responding firms. Mercer may calculate worldwide assets under advisement and worldwide assets under management differently than other responding firms. The assets under advisement data (AUA Data) reported here include aggregated assets under advisement for Mercer (Canada) Limited, Mercer Global Investments Canada Limited, and their affiliated companies globally (Mercer). The AUA Data have been derived from a variety of sources, including, but not limited to, third-party custodians or investment managers, regulatory filings, and client self-reported data. Mercer has not independently verified the AUA Data. Where available, the AUA Data are provided as the date indicated (the Reporting Date). To the extent information was not available as of the Reporting Date, information from a date closest in time to the Reporting Date, which may be of a date more recent in time than the Reporting Date, was included in the AUA Data. The AUA Data include assets of clients that have engaged Mercer to provide project-based services within the 12-month period ending on the Reporting Date. The assets under management data (the AUM Data) reported here include aggregated assets for which Mercer Global Investments Canada Limited and their global affiliates provide discretionary investment management services as of the dates indicated.

Investment management services for Canadian investors are provided by Mercer Global Investments Canada Limited. Investment consulting services for Canadian investors are provided by Mercer (Canada) Limited.