Capital Group CEO Tim Armour on weathering the coronavirus

KEY TAKEAWAYS

- News of the continued spread of coronavirus – and the recent plunge in oil prices – has sent stocks plummeting toward bear market territory, and bond yields have reached unprecedented lows.
- While the virus represents a new challenge, there is nothing new about market volatility. Markets have survived viral outbreaks in the past.
- Investors who can look past the current environment and stay the course can benefit over the long run.

Rising fears over the continued spread of the coronavirus have led to a sharp stock market decline as investors grapple with its impact on the global economy. On Monday, March 9, in reaction to news of the virus spread and the recent oil shock, Standard & Poor's 500 Composite Index fell 7.6%, triggering a 15-minute trading halt. In this interview, Capital Group Chairman and CEO Tim Armour offers his perspective on the latest events and what Capital is doing in portfolios to help guard against market volatility.

1. What is your sense of the coronavirus (COVID-19) outbreak and market reaction?

Until January 2020, most of us had never heard of this virus. In short order, we have grown increasingly concerned about the prospect of its impact on the global economy. People are understandably frightened because this is a new disease, and there is much uncertainty over how it will all play out. First and foremost, the virus has a real human cost. We don't know how many people are going to get ill or, worse yet, how many may die. Of course, our first thoughts are with the people who have fallen ill and their families.

While this disease is new, there have been many viral outbreaks and other crises in the past, and markets have survived them all. Today, a fair amount of panic has taken hold around the world, and I expect in the coming weeks that a rising number of cases may alarm many people. As an organization, we have been studying the history of outbreaks and the pattern they have tended to follow. There have tended to be hot spots and flare-ups, and they lasted for a while, but then they went away. Eventually, the spread of the virus will slow down and people will get back to normalcy, as will markets.

2. What does this mean for the economy?

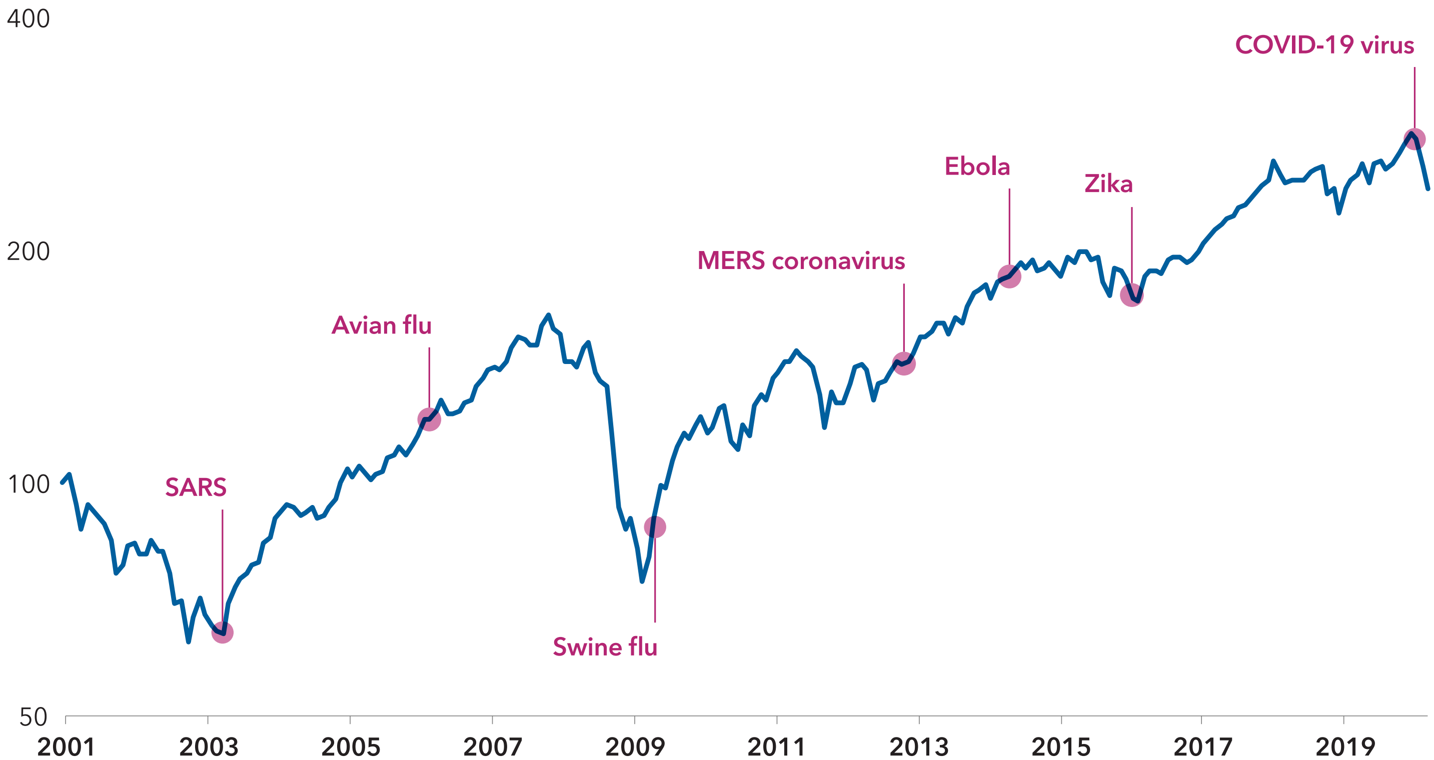
We are already seeing signs of a slowdown in the U.S., not only on the supply side as businesses brace for the road ahead, but also on the demand side. By now we have all heard of large conferences and entertainment events being canceled, firms postponing large meetings, and consumers delaying vacations and seeking to reduce their social contact.

That means businesses related to travel, leisure, entertainment and recreation are likely to be the most impacted, not to mention oil and other commodities where we have already seen a collapse in global demand. A U.S. recession has become increasingly likely. We could see corporate earnings turn negative in the first quarter, which would continue to dampen investor sentiment.

On the positive side, the U.S. economy remains among the most resilient in the world. It has a history of bouncing back from adversity. Interest rates are low, and the decline in oil prices should further support the consumer. What's more, in

Global equity markets have powered through past viral outbreaks

MSCI ACWI index levels



Sources: Centers for Disease Control and Prevention, RIMES, MSCI. As of 3/9/20. Chart shown on a logarithmic scale. Total return index levels in USD, indexed to 100 on 31/12/2000. Disease labels are estimates of when the outbreak was first reported.

China the spread of the virus appears to have peaked. Given that, I think the peak of its spread globally will occur sooner than many people anticipate.

3. What does it mean for markets?

We are experiencing a market decline that we have not seen since the Global Financial Crisis. As I speak today, March 9 is the 11th anniversary of the market bottom during the Global Financial Crisis – and the market noted the anniversary by recording the largest single-day point decline we have ever seen.

As of the market close on Monday, the broader equity markets, as measured by the S&P 500, were down nearly 19% from their peak earlier in the year, and we may soon be in bear market territory, which is defined by a decline of more than 20%.

This would be the first bear market after more than a decade of generally strong market returns. As a result, in general, equities appeared to be fully valued by most measures heading into this recent period, and markets could remain volatile for some time. In addition to the uncertainty resulting from the spread of the virus, the U.S. is in an election year.

Turning to the bond market, we have seen a flight to safety that has pushed bond yields to unprecedented lows. The yield on the 10-year U.S. Treasury fell to 0.5%. Interest rates could go still lower as the U.S. Federal Reserve seeks to provide liquidity to markets through interest rate cuts and quantitative easing. Over time, low interest rates provide support to equities.

While the pace and magnitude of the recent volatility can be unsettling, it is not entirely surprising. Investor sentiment is fragile and will likely remain so until the spread of the virus slows. In times like these, resilient investors who can demonstrate patience can be rewarded over the long term.

I take some comfort in seeing that the Federal Reserve has demonstrated its willingness to take aggressive action, cutting interest rates 50 basis points in an emergency meeting on March 3, which lowered its target range to between 1.00% and 1.25%. The Fed stated that it is “closely monitoring developments and their implications for the economic outlook, and will use its tools and act as appropriate to support the economy.” Markets are generally expecting an

Market downturns happen frequently but don't last forever

Standard & Poor's 500 Composite Index (1950–2019)

Size of decline	-5% or more	-10% or more	-15% or more	-20% or more
Average frequency*	About three times per year	About once per year	About once every four years	About once every six years
Average length†	43 days	112 days	262 days	401 days
Last occurrence	August 2019	December 2018	December 2018	December 2018

* Assumes 50% recovery of lost value.
† Measures market high to market low.

Sources: Capital Group, Standard & Poor's.

additional cut at the Fed's next scheduled meeting, to be held on March 17 and 18.

4. How does this compare with crises in the past?

In the 37 years I have spent as a professional investor at Capital, I have experienced a number of unsettled markets, including the savings and loan crisis in the late 1980s, the tech and telecom bubble that ended in March 2000, and the Global Financial Crisis of 2008 and 2009. Each of these crises was very different, with very different underlying conditions. But in each case, the markets bounced back. I believe the markets, and great companies, will survive the current market decline and rebound.

Let me share with you the words of two of my predecessors who mentored me through periods like this. Jim Fullerton, as Chairman of Capital in 1974 in the depths of one of the worst bear markets we have ever seen, wrote these words that are relevant today:

"One significant reason why there is such an extreme degree of bearishness, pessimism, bewildering confusion and sheer terror in the minds of brokers and investors alike right now is that most people today have nothing in their own experience that they can relate to, which is similar to this market decline. My message to you, therefore, is courage! We have been here before. Bear markets have lasted this long before. Well-managed mutual funds have gone down this much before. And shareholders in those funds and the industry survived and prospered."

And Jim Rothenberg, former Chairman of Capital Group, said this amid the Global Financial Crisis in 2008:

"I have seen many turbulent markets and know how hard it is to avoid getting caught up in the here and now. This is especially true when the media bombards us hourly with news, speculation and rumor. I also know, though, that as long-term investors we must focus on the real world underneath the noise and mesmerizing flow of data."

5. Should investors expect a quick recovery?

At this point, I do not think it is realistic to expect a quick recovery. Circumstances may very well get worse before they get better. But I believe eventually markets will rebound. This too shall pass. When it does, long-term investors who can tune out the daily white noise – and red numbers flashing across their screens – and focus on the long term should ultimately be rewarded.
I take the view that we will deal with outbreaks like COVID-19 and eventually we will adjust to it. At Capital, we are taking every precaution to prepare for it. We expect that we will be dealing with the COVID-19 virus for some time, possibly a year or two.

One further point: We have offices in Singapore, Beijing, Hong Kong and Tokyo with a significant number of associates. They have already lived through four weeks of COVID-19. In China, people are already starting to go back to work. If you look at our associates in these offices, they were dealing with an emergency a month ago and today they are returning to a less disruptive life and business environment. They feel things are much more under control. I look at that as a pattern we are likely to experience here in the U.S. and Europe at some point.

6. What are you doing in your portfolios now to guard against market volatility?

Our company was founded in 1931 in

the depths of the depression, with the aim of managing investment mandates designed to do well in volatile market periods. We seek to protect our investors' capital on the downside, and we invest for the long run. I recently looked at our funds' results during this admittedly brief period of turmoil. If you look, you will find that many of our U.S. funds have done what we aspire for them to do: They have held up relatively better than their primary benchmarks (as of March 9, 2020).

7. What is CG doing to ensure continuity as we take care of client assets?

Obviously our first concern is to ensure the health and safety of our associates. We hope the same for investors and advisors. But rest assured as this situation evolves, our more than 350 investment professionals in offices around the world continue to do what they have always done: analyzing companies and making real-time judgements about their potential long-term value. In-depth, fundamental research and a long-term view of markets is at the core of what we do. We will do our very best to provide investors with a smooth and less volatile experience than the broader markets.

8. What should investors be doing?

In periods of declining markets, emotions run high, and that's natural and understandable. But it is exactly in times like this that a long-term orientation is important. Based on my prior experiences and what has historically occurred, I firmly believe markets will rebound and life will return to normal. Now more than ever, investors should be in close communication with their advisors, reaffirming their long-term objectives.

Tim Armour is chairman and CEO of Capital Group, as well as an equity portfolio manager. He has 37 years of investment experience, all with Capital. He holds a bachelor's in economics from Middlebury College.

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Standard & Poor's 500 Composite Index is a market capitalization-weighted index based on the results of approximately 500 widely held common stocks.

The MSCI ACWI is a free float-adjusted market capitalization-weighted index that is designed to measure equity markets results in the global developed and emerging markets, consisting of more than 40 developed and emerging market country indexes.

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