

# UPDATE ON THE CURRENT VOLATILITY IN EQUITY MARKETS



PERPETUAL ASSET MANAGEMENT  
11/03/2020

The continued global spread of the coronavirus has led to concerns about the sustainability of global economic growth and sparked a major sell off in markets, which had already been trading at elevated levels. Selling has been indiscriminate.

The Perpetual Investments Equities teams continue to assess the impact of the coronavirus on the economy and our clients' portfolios. Whilst the severity and duration of coronavirus is still unknown, it is important to remember that the Perpetual investment philosophy and process focus on buying high quality companies at prices below what we perceived as fair value, based on company fundamentals and prevailing market conditions. The starting point of this investment approach are our quality filters.

All prospective Perpetual Investments must pass these four filters which screen for:

1. Quality businesses,
2. Sound management,
3. Conservative debt, good balance sheets (low, or no, corporate debt)
4. A track record of recurring earnings.

Furthermore, any company that passes our quality filters must then be rigorously assessed for value. Companies that we think are undervalued relative to their potential are then included in the portfolio.

Given that the coronavirus will likely affect multiple industries in the months ahead, the fact that our portfolios are comprised of profitable businesses with quality balance sheets, trading at reasonable valuations, ensures that they are better equipped to handle volatility arising from the current situation.

**As an example of this is Crown Resorts (Crown or CWN).**

Crown, like many companies, will be operationally affected as the coronavirus expands over the course of 2020. When considering the impact on Crown's earnings, close assessment is given to the exposure of the business to tourism and domestic visitation. Whilst this will clearly have an impact on the earnings for Crown over the short term, we must also consider that Crown has long dated licences (including a 100 year licence in Sydney) and hard assets that will continue generate strong earnings well after the coronavirus has passed.

The new Crown Sydney casino opens in 2021/2, by which time Crown will be virtually debt free. At this time, Crown will have ended a capital investment phase and will start to generate significant amounts of free cash flow. The under-g geared balance sheet together with the strong free cash flow provide the company with significant balance sheet optionality that may see them conduct a highly accretive buy-back.

Crown has exactly the characteristics we like; secure earnings streams, hard assets, monopolistic businesses (licences that restrict competition) and a quality balance sheet.

The stock price has fallen, along with the market, in the last few weeks. Is it reasonable though, to heavily discount the value of a company with such a strong balance sheet and earnings outlook because of short term traditions? We have already assumed that their VIP and mass business declines sharply in 2020. Yet the stock continues to look attractive on a long-term view.

**Conclusion**

Despite the fear and impact of the coronavirus, our key focus is to be aware of the risks that are currently gripping markets, but also to maintain perspective. Crises can be painful, but they also bring opportunities. We must be mindful of the latter as well as the former.

**➤ FURTHER READING - COVID-19**

Visit our COVID-19 Insights Hub for economic and market updates to keep you informed as the situation evolves.