BKCoin Capital

Market Commentary: March 2020

Initial Stages of the Outbreak - December 31, 2019 - February 11, 2020

On December 31, 2019, Chinese Health officials inform the World Health Organization that 41 people had contracted a mysterious pneumonia in Wuhan, China. Thinking that the outbreak originated from a popular Huanan Seafood Wholesale Market, a day afterward, Chinese officials issue an order to close the Huanan Seafood market. In the following two weeks, officials identify the virus as a new strain of the Coronavirus. On January 11th, China records its first death linked to the virus outbreak. Both society and financial markets remain unreactive during the initial stages of the outbreak. US equities continue their post-global financial crisis bull market, meanwhile, digital asset markets get squeezed signalling to investors that digital asset markets could potentially rally into bitcoin's halving. In credit markets, high-yield remains stable and US Treasuries sell-off of their recent highs stemming from post-China US trade war anxieties.

Chart 1.0: *US Equities continue their bull run into 2020.* Nasdaq100 (Orange), SPX(Blue) and DIA (Red).

Chart 2.0: *Rallying off a short squeeze.* Bitcoin (Blue) and Alt-Markets (Red)

Chart 3.0: *Treasury coming off its recent highs & high-yield remains stable.* US Treasury 20 YR bond (Red) and high yield (Blue)

On January 13th, a citizen in Thailand contracts the new strain of the Coronavirus rendering this the first case outside of China. A week later, the epicentre of the outbreak, Wuhan, which has a population of 11 million people, is placed under quarantine. Several days later, the Hubei Providence, which has a population of five times that of Wuhan, is also placed under quarantine. As the pandemic shakes the social lives of tens of millions of Chinese citizens, financial markets in China begin to crack. FXI, which tracks large-cap Chinese companies, diverges from the S&P 500 by approximately -11%. While FXI bulls fail to make new highs, US investors propel the S&P 500 to new all-time highs.

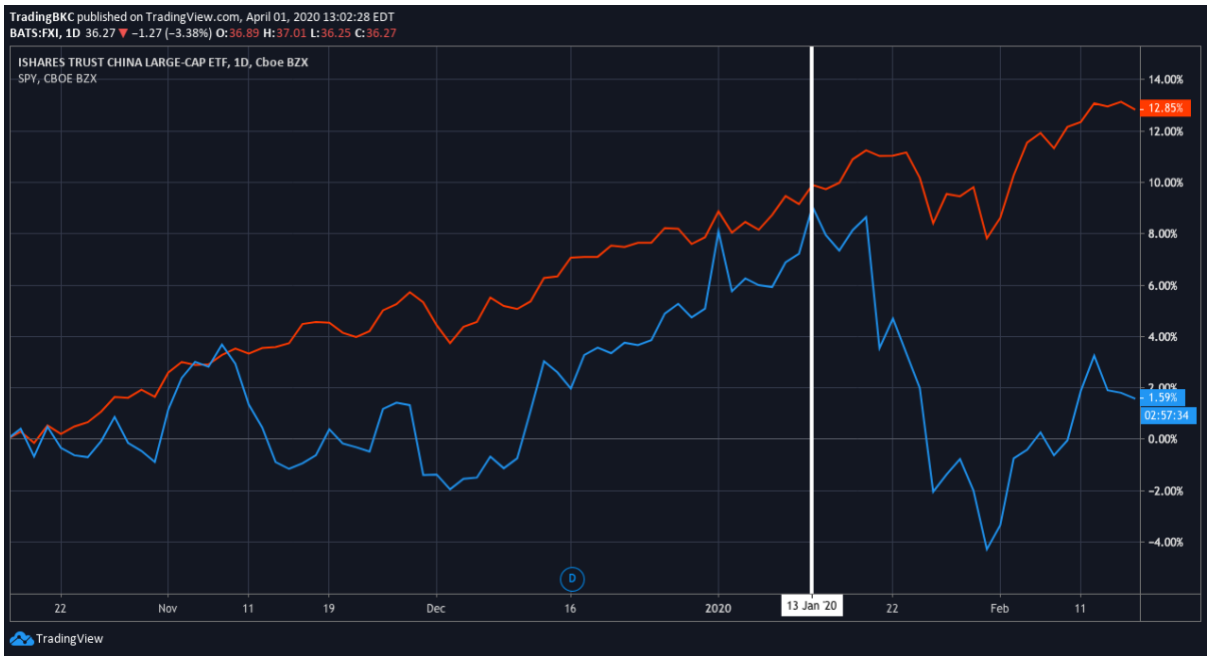

Chart 4.0: *FXI diverges from the S&P 500 as the outbreak accelerates in China.* FXI (Blue) and S&P 500 (Red)

During the first week of February, a citizen from the Philippines dies from the virus rendering it the first death linked to the virus outbreak outside of China. Soon afterward, the first American citizen, who was residing in Wuhan, also dies from the virus. With over 1,000 deaths recorded, the death toll in China surpasses that of the SARS epidemic. By February 11th, 45,000+ virus outbreak cases are confirmed across the world and the World Health Organization (WHO) dubs this epidemic "COVID-19."

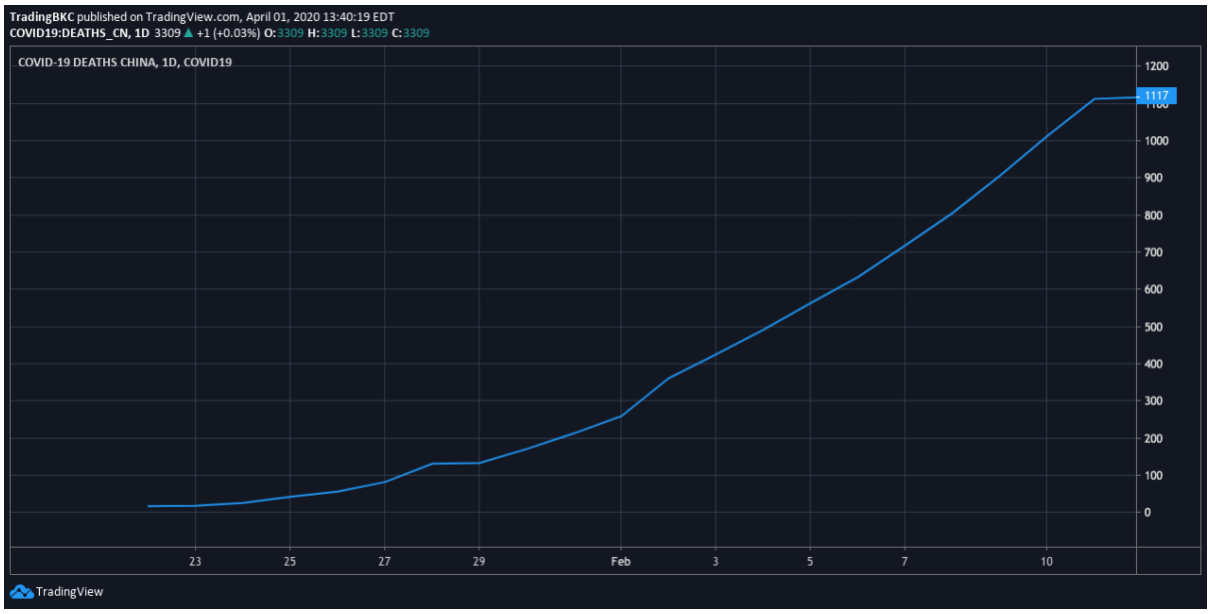

Chart 5.0: *Death toll in China from COVID-19 passes that of the 2002-2003 SARS epidemic*.

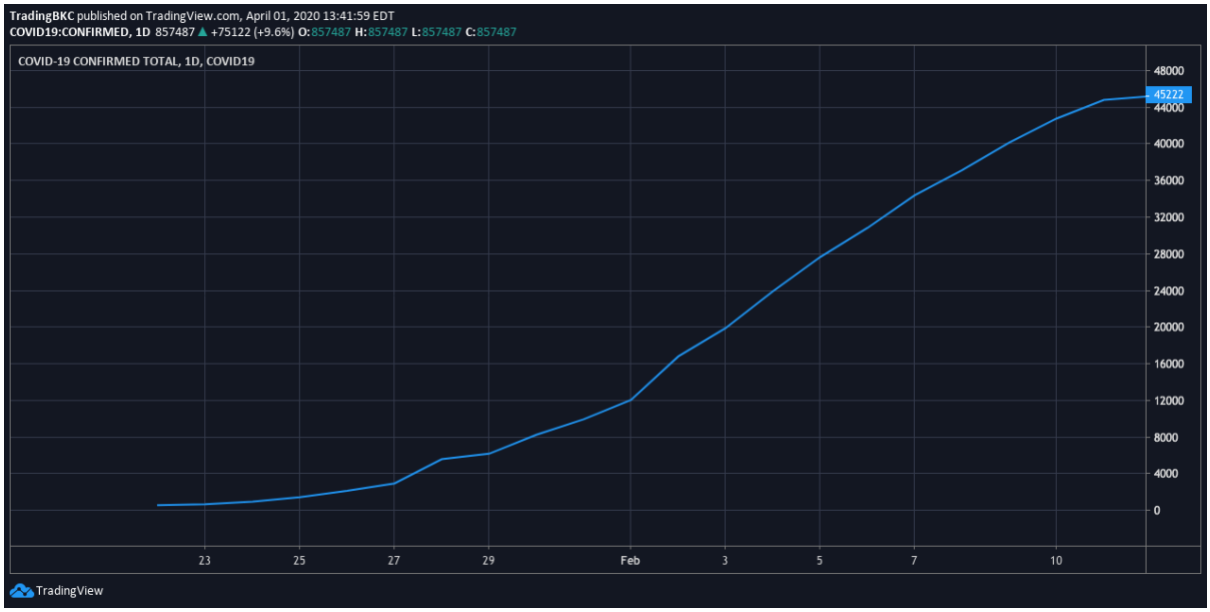

Chart 6.0: *Over 45,000 COVID-19 cases are confirmed worldwide*.

The Epidemic Becomes a Pandemic: February 12, 2020 - March 3, 2020.

In a span of less than a month, the virus permeates throughout the world. On February 12th, COVID-19 cases begin to spike in South Korea. Global anxieties finally begin to materialize causing the S&P 500 to join FXI in the COVID-19 sparked sell-off.

Chart 7.0: *S&P 500 sells off along with FXI*. S&P 500 (Red) and FXI (Blue).

A week later Iran and Italy face major outbreaks rendering the Chinese epidemic a global pandemic. Realizing that the outbreak will have long term devastating effects on global markets, institutional investors initiate the first wave of selling of "risky" assets. By the end

of February, almost all global equity markets are down double digits year to date.

Chart 8.0: *Almost all equity markets are down double digits for the year 2020.*

Meanwhile, as investors abandon equities, they flee to safe-haven assets, marking a shift from a risk-on to a risk-off investment environment. Both Gold and Treasuries are aggressively bid up by institutions.

Chart 9.0: *Gold and Treasury Notes rally as investors flee to safe-haven assets.*

The capital flow from risk-on assets into risk-off assets also manifests bitcoin's current status in global markets with equities and high yield, rendering the digital asset amidst the selloff to be strongly correlated to risk assets and inversely correlated to safe-haven assets.

Chart 10.0: *Bitcoin loses its safe-haven status as rolling 20-day correlations show that bitcoin is strongly correlated with risky assets (Equities & High Yield) during the sell-off and anti-correlated with risk-off assets (Gold and Treasuries) during the selloff.*

Hoping to qualm global markets, Central Banks around the world initiate liquidity injections into financial markets. **On March 3rd,** the Federal Reserve makes its biggest single interest rate cut in more than a decade cutting interest rates by half a percentage point and targeting a Fed Funds rate between 1 and 1.25 percent. Smart money anticipating the cut, cover some of their short positions into the news sparking an almost 10% bounce in the S&P 500.

Chart 11.0: *Smart Money covers into the drop, sparking a small rally in the S&P500.*

However, the bounce would be short-lived and the drastic monetary policy measures taken by the Fed would be deemed futile. The unprecedented financial and social damage would spark complete fear-induced capitulation across global markets.

The Apocalypse: March 3, 2020 - March 28, 2020.

In just three days, the dead cat bounce in the S&P 500 fades as more negative news about COIVD-19 is manifested. Spain announces a spike of cases within their country and the global infection count totals over 100,000 people and 3,000 deaths are recorded.

Chart 12.0: *Over 100,000 COVID-19 cases are confirmed.*

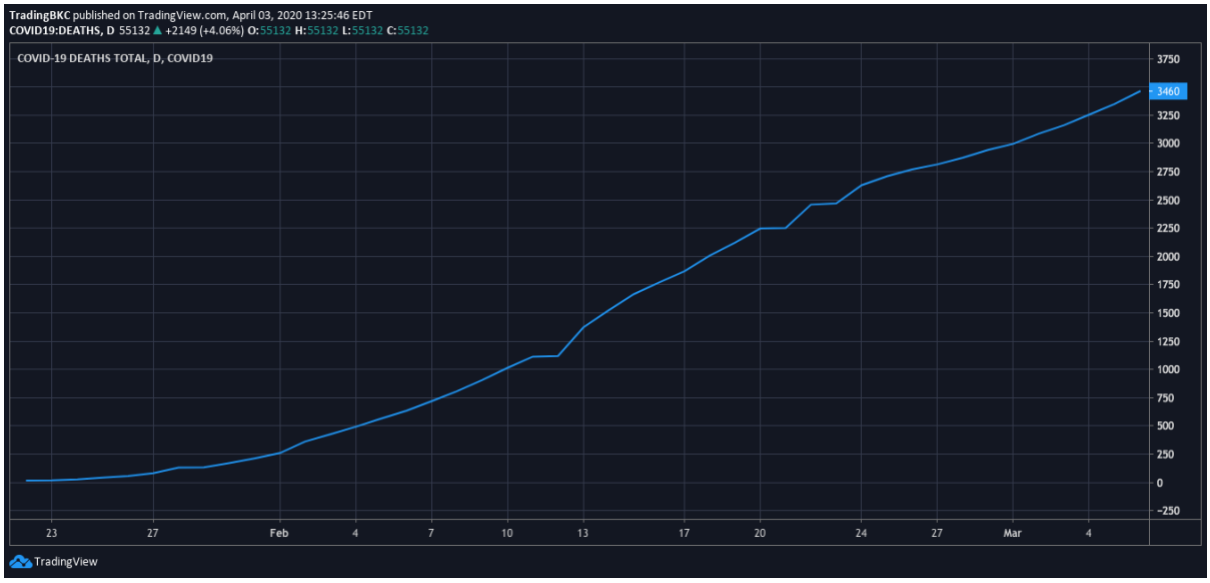

Chart 13.0: *Over 3,000 lives are lost from the virus.*

Chart 14.0: *S&P 500 "dead cat bounce" fades.*

As the outbreak continues to worsen, a completely idiosyncratic crisis occurs in energy markets during the first weekend of March as a Russia-Saudi Arabia oil price war commences. This causes traders to panic sell oil in anticipation of a glut of oil flooding energy markets. **On Monday, March 9th**, the price of crude oil opens down more than -20% dragging down both US equities and high yield.

Chart 15.0: *Crude oil loses +24% in one trading session*.

The price of crude oil futures loses around 24% on the day, and almost -9 sigma move based on annual historical volatility, rendering it the largest drop in the crude oil market in the last 40 years.

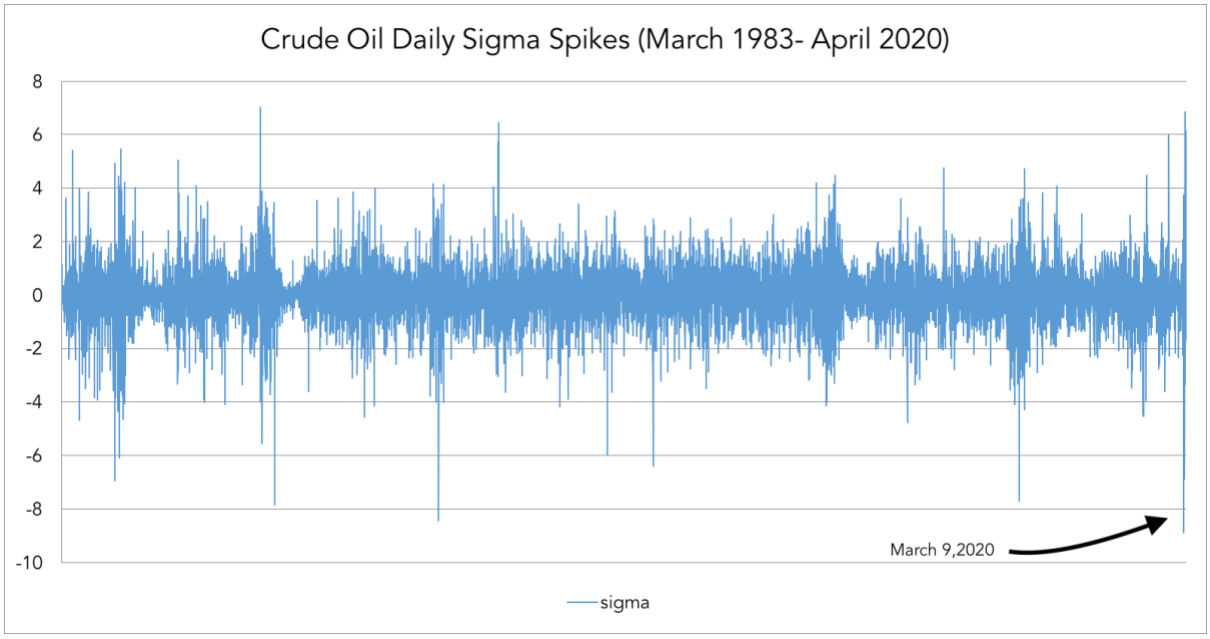

Chart 16.0: *Crude oil's percent change in price from previous day's closing price to the most recent days closing price rebased in terms of annual volatility.*

In the weeks following the crude oil price collapse, global markets around the world capitulate as the collapse in energy markets is only one of several negative materializations that continue to exacerbate the sell-off. Italy places its entire country on lockdown, the World Health Organization officially declares the virus a global emergency and the US declares a national emergency. Realizing this was just the start of the panic-induced capitulation, central banks around the world begin taking unprecedented stimulus efforts in order to combat the systematic collapse. **On March 15th**, the Federal Reserve decides to cut rates to zero and launches a $700 billion quantitative easing program.

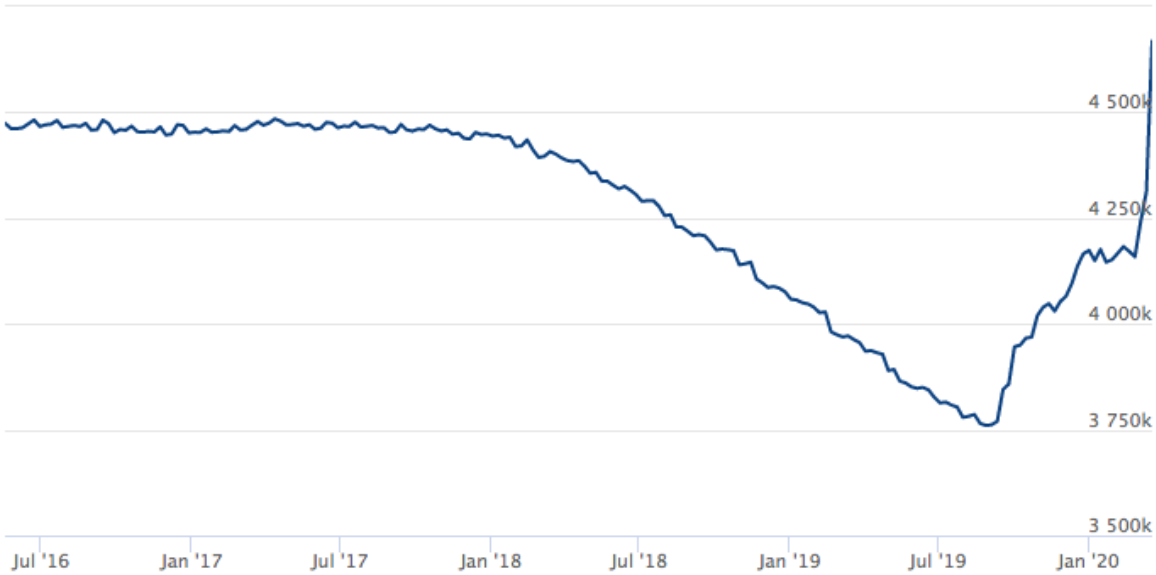

Chart 17.0: *Fed QE balance sheet expansion. Fed's assets under management reach all-time highs as the Fed's balance sheet reaches almost $5trillion.*

The Federal Reserve's efforts are futile and by **March 23rd**, all major global equity indices are down more than -20%.

Chart 18.0: *All major global equity markets down more than 20% for 2020.*

The Dow Jones Industrial Average, the hallmark of US blue-chip investments, suffers a peak to trough decline of around 37%, marking this the fastest and steepest drop in the index since the Wall Street crash of 1929.

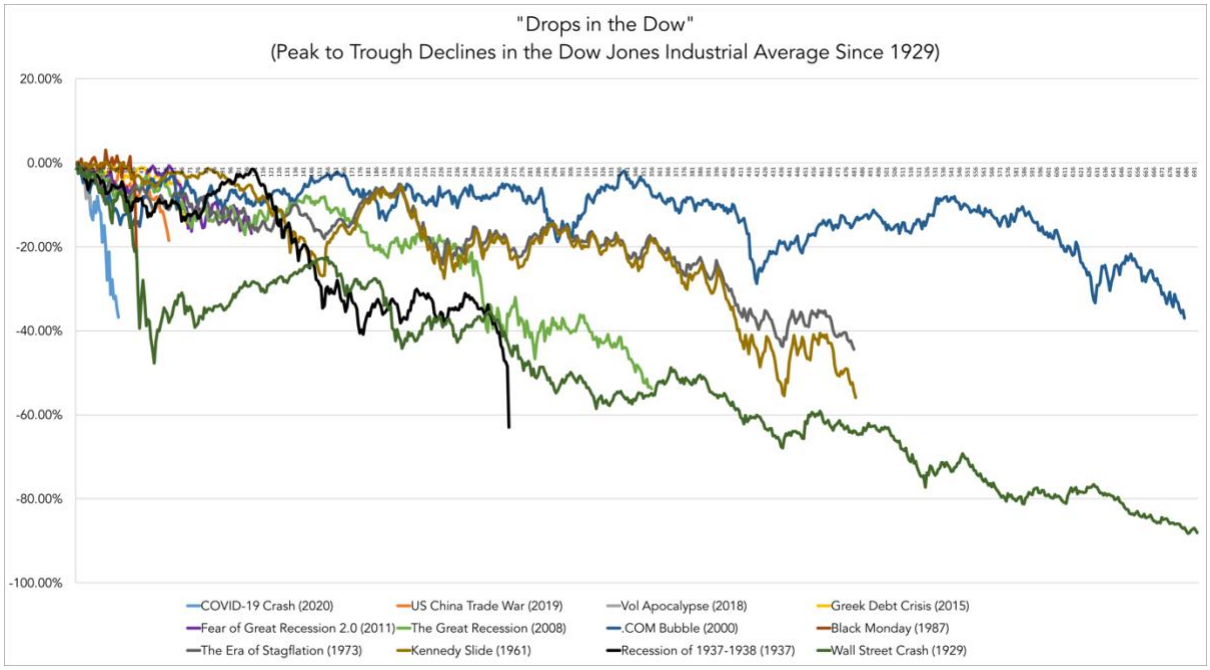

Chart 19.0: *Drops in the Dow Jones Industrial Average since 1929.* The X-Axis measures the drop from the peak to trough during a market sell-off. The Y-axis measures the severity of the drop in %. Until the Dow makes a new all-time high the bottom (trough) is still undefined.

In currency markets, the demand for dollars soars as emerging market investors aggressively sell off emerging market currencies.

Chart 20.0: *Investors aggressively bid up the dollar against emerging market currencies.*

In credit markets, high yield encounters its steepest losses since the Global Financial Crisis.

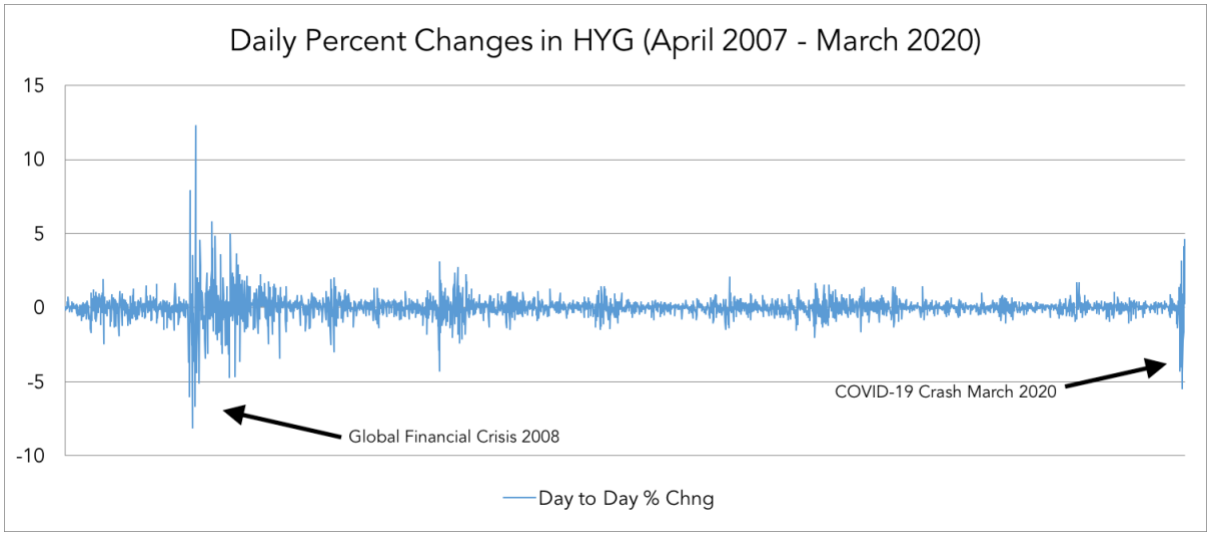

Chart 21.0: *Daily Percent changes in HYG*. The HYG is an ETF that tracks high yield credit.

In digital asset markets, bitcoin suffers the worst daily drop in its history, losing around 38% against the dollar in an individual trading session.

Chart 22.0: *Bitcoin's largest single-day loss against the dollar.*

To end the month of March, hoping to salvage the US economy, the US government passes the largest fiscal stimulus package in the history of the United States. The $2 trillion stimulus package provides emergency funding for businesses and direct payments for US households. Although March 2020 will be remembered as one of the worst months for global financial markets, the largest losses came from lives, not dollars. Sadly, to end the month of March, over 900,000 people would be infected and over 46,000 deaths would be recorded due to COVID-19.

Chart 23.0: *Over 900,000 COVID-19 cases confirmed to end March 2020.*

Chart 24.0: *Over 46,000 lives lost from COVID-19 by the end of March 2020.*

Sources:
Business Insider: Coronavirus outbreak timeline
TradingView: Charts
FRED: Federal Reserve and US Government policy