

## Beyond the coronavirus

### Close Inheritance Tax Service



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In four short months, a previously unknown coronavirus has spread from a market in Wuhan, China, across the entire world. The pandemic has caused an unprecedented global lockdown. As the responses of governments, central banks and other authorities were at first considered insufficient, shares went into freefall and headed towards their quickest ever bear market. A rush for dollars (momentarily at least) caused many other assets to be liquidated. Hard panic had set in.

While this has been unnerving for investors, it's more important than ever to remain calm and place current events in their historical context. Coronavirus has ended a decade-long bull run for global equities, but at some point the bull will return.

In the **Close Inheritance Tax Service**, we were already trading cautiously going into the bear market. By the end of 2019, some companies we owned in the service were acquired and when looking to reinvest the windfall, it was tricky to find what we considered good value for investors. Our response to the coronavirus has been to work tirelessly to protect the value of every pound clients have entrusted to us. This includes engaging with the companies we own that may be challenged by the outbreak.

Among others, we need to focus on companies with high net liabilities and those seeing their working capital unwind:

- Those which may have to stop or drastically cut their dividends
- Those which may need to raise capital (which would dilute our equity)
- Those which have high net debt/EBITDA ratios (are too leveraged)
- Those at risk of being nationalised 'by the back door' via conditional government loans, which may later be converted to shareholder equity

In the face of some of the most extreme trading conditions we have ever seen, we have forensically analysed balance sheets, liquidity and debt profiles to develop a list of companies which we believe will emerge stronger from this downturn. These are ones with either net cash or manageable levels of debt and good, consistent revenue over time (often family/founder-led businesses).

Because these types of companies are so popular, they usually trade at a high premium – something compounded by the prolonged bull market. With the recent sell-off, there will be opportunities to pick up companies that have been oversold, with the potential to generate good returns for investors. Our job now is to remain focused on what is ahead.

With the adage 'never catch a falling knife' in our minds, we are continuing to take a cautious view when allocating capital, even if we are likely to increase the number of holdings to the top end of our usual 25-35 range. We will add to portfolios incrementally and in smaller position sizes until we reach a comfortable standard size. The current market offers an attractive entry point for long-term investors, however with high volatility companies can be mispriced in the short-term.

We have always maintained a conservative investment approach and although this means we might not see the highest of the highs, historically it has meant that we have avoided prolonged lows when the market hits a difficult patch – as is happening now.

For Business Relief this is important. Investors are in it for the long-haul and, generally, do not know exactly when their estate is going to need to claim the relief. That's why we aim to smooth out the short-term pain and protect as much of their 40% head-start on Inheritance Tax relief as possible.

The recent shocks have demonstrated the benefits of preparing for a downturn, even when times are good. A number of years ago, we invested in a pawnbroker and an insolvency practise which we believe will provide some growth for investors while other businesses struggle.

Not being too greedy, we've always preferred to avoid the excesses of the bull market by never overpaying for companies.

Finally, the key is not to panic. It's difficult to know all the long-term consequences of the coronavirus, but people are adaptable. Our strategy beyond this outbreak is unchanged – that is to pay attention to company balance sheets, look for value and build well-diversified portfolios for investors.

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