



SIX TRENDS OF A POST-COVID-19 WORLD

We're living through history. The Covid-19 experience will be distinctly pivotal for humanity. Like the impact of World War II or 9/11, societal priorities may change significantly. While the world fights a disease, rather than fascists, the battle is for our way of life.

The inertia of the world is a powerful force. Most predictions of radical change prove wrong. That said, the longer this impacts the current way of life, the greater the chances of emerging into a different world. Our investment team put together the following analysis of six trends that may arise in a post-Covid-19 world.

Trend 1: "Don't Break the Chain"

Coming off the China trade war, many companies were beginning to examine their supply chains. After nearly twenty years of cost savings, manufacturers have concentrated operations in China. What started as a strategic examination of supply exposure is turning into an operational imperative. Even in the case of a quick recovery from the pandemic, countries across the globe will be reinforcing critical food service and medical supply chains. Industries worldwide will be moving quickly to avoid fallout from another disruption.

The magnitude of the supply chain transformation could be massive. 94% of Fortune 1000 companies are experiencing disruptions to their supply chain as a result of the Covid-19 pandemic.¹ Rich countries could see economic gain from onshoring of manufacturing whose cost savings abroad are no longer worth the risks. That said, we would expect new highly automated factories to hire fewer workers. Companies may additionally spread manufacturing across multiple locations. We could even see a reversal from "just-in-time" manufacturing as companies hold higher levels of inventory as a contingency. These strategies could lead to increased costs for consumers.

The biggest losers from this trend will be developing countries. Poor countries have long used their cheap labor as a path to development through manufacturing. The loss of this employment could be devastating for emerging economies. Thomas Friedman's Dell Theory stipulates that no two countries that are part of the same global supply chain (like Dell computers) will go to war. The "de-globalization" of supply chains may lead to more international conflicts.

Trend 2: "A Contingency Plan for our Contingency Plan's Contingency Plan"

Heading into 2020, no one was ready for a global shutdown. Unlike past recessions, the pandemic offered no warning signs. This resulted in a surprise game of musical chairs. When the music stopped, many were left without a chair. Companies with recent acquisitions, aggressive growth plans and/or stock buy-backs are suddenly over-levered and cash poor. Governments lack medical stockpiles, testing plans, and healthcare capacity. While consumer savings rates have remained elevated since the Global Financial Crisis², a shocking number of Americans have no jobs or savings.

¹Fortune Magazine, February 21, 2020: <https://fortune.com/2020/02/21/fortune-1000-coronavirus-china-supply-chain-impact/>

²Statista.com: <https://www.statista.com/statistics/246234/personal-savings-rate-in-the-united-states/>

Preparation for the “next” pandemic will be society’s focus as we emerge from Covid-19. Governments will form new Bureaus of Public Health tasked with surveillance of potential viral outbreaks. Government warehouses will fill up with stockpiles of emergency medical supplies. Rating agencies will perform new stress tests on companies to assess their ability to survive a shutdown. Consumer savings rates will increase to provide middle class families with an emergency backstop. The deeper the Covid-19 recession, the greater the resulting contingency plans. This provides a competitive advantage to larger, incumbent businesses with fortress-style balance sheets. The safety of these businesses is more attractive for capital allocators over poorly capitalized, but dynamic start-ups.

Trend 3: Virtual (not) Reality

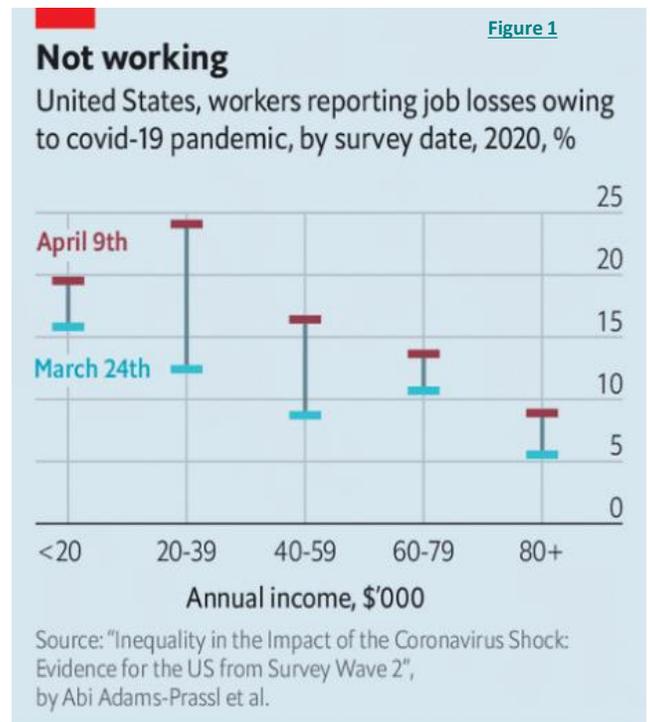
After weeks of home quarantine, connections to the outside world are increasingly virtual. Usage rates on social media and virtual work applications have skyrocketed. “Work from home” is no longer an experiment. While working from home might be seamless for some and unproductive for others, it is now an acceptable option for employers. Taken to an extreme, this could lead to big changes in hiring with companies sourcing the most efficient, skilled workers in the world, regardless of location. As companies adopt virtual resources, they could move to a future of shared labor. On the flip side, the movement towards shared capital could reverse. In a post-Covid-19 world, consumers will feel safer having a stranger deliver them dinner than eating dinner off a stranger’s table. Physical sharing is suddenly uncomfortable.

Trend 4: Urban Flight 2.0

Following World War II, middle-class Americans fled urban cities for the space of suburban yards and single-family homes. More recently that trend reversed as Millennials flocked to the convenience of apartment living in urban city centers. With New York and other urban centers suffering the worst of the pandemic, it’s increasingly clear that density comes with health risks. The most recent census data has shown residents leaving California and the Northeast as housing prices push middle class workers to cheaper Sun Belt cities. The pandemic could accelerate this trend. As the virtual world provides the convenience of work from home and grocery delivery, could we see a retreat to suburban or even rural living?

Trend 5: Enter Big Government

In 1986 Ronald Reagan said, “The nine most terrifying words in the English language are: I’m from the government and I’m here to help.” Today, many Americans are welcoming those words as the government provides \$6 Trillion of fiscal and monetary support. While the data is still coming in, it appears that lower income workers are suffering massive job losses (Figure 1). Some economists are predicting unemployment in excess of 20% within four weeks. Given the expected shift towards automation, social distancing and virtual services, we don’t know if or when these jobs will come back. Governments will try to spur employment through large scale infrastructure spending. Reversing the income disparity of post-2008 policies, stronger countries may implement a broad expansion of entitlements for lower income citizens. The economic damage could be even more pronounced in emerging market economies. We could see a full-blown wave of populist revolutions. Faced with disease, hunger, and hopelessness, revolutionaries could drive weak states into lawlessness.

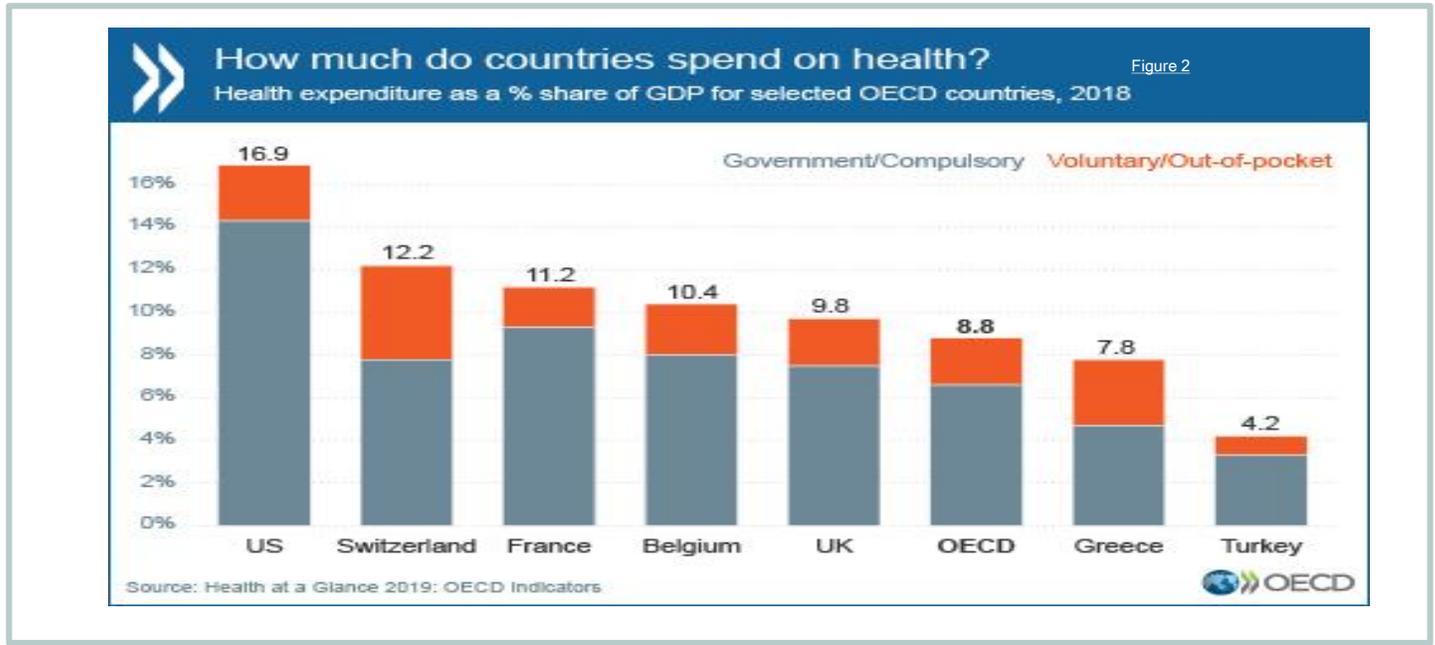


The Economist

³US Census 2019: <https://www.census.gov/library/stories/2019/04/moves-from-south-west-dominate-recent-migration-flows.html>

Trend 6: Healing Healthcare

What is the purpose of government? Modern society expects government to provide for our health, security, and property rights. In the 1940s, the US government borrowed massively to defend the free world against fascism. The policy continued during the Cold War. Now, we have borrowed again to fight a new war against the Covid-19 virus. While healthcare policy has recently divided our country, the war against Covid-19 may reframe the debate. Compared to other OECD countries, the waste and inefficiency in the US healthcare system is tremendous (Figure 2).



By monitoring and surveilling the population for future pandemics, we could refocus our system on preventative care as well as on cost savings. If the coronavirus is resolved quickly, do we focus on national contingency planning for future pandemic-level peak usage? If we struggle with the current pandemic for some time, do we partially socialize our healthcare system to guarantee a basic level of care for all citizens?

Conclusion

These six trends are long term forces that will shape client allocations for years to come. The existing BFO investment themes of automation, payment technologies, and biotechnology will likely emerge from this crisis with stronger tailwinds. Once promising investments in emerging markets and energy now appear to be risky. Current distressed opportunities exist in structured credit markets, while future distressed opportunities will present themselves in real estate and private debt.

Gazing into the crystal ball of a post-Covid-19 future, shadowy trends appear through the clouds. That said, these are early days. No one knows the length, the severity, or possible reoccurrences of the pandemic. Given the unknown impact of the shutdown on human behavior, government policy, and capital markets, patience will be critical when making long-term allocations. These six trends provide us with a framework to view our shifting investment landscape. While considering various severities, the following analysis offers example winning and losing investments by trend.

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Post-Covid 19 Trend Summary

Trend	Description	Low Impact	Medium Impact	High Impact	Winners	Losers
Don't Break the Chain	Onshoring & supply chain redundancy. Increased automation and social distancing.	Lesson learned - supply chains are reinforced. Onshoring in key industries - food service, healthcare. Continued slow trend towards duplicating suppliers with geographic diversity.	Accelerated move of manufacturing from Asia to America. Retail RE conversions to industrial distribution. Increased inventories for contingency.	Inefficient manufacturing. Borders pose challenges to global supply chain. Unwind of "just in time" manufacturing. Whole industries moved onshore. Possible inflation.	Industrial CRE, Automation, US & European manufacturing	Outsourced manufacturing, Emerging markets, Shipping, Consumers
Contingency, Contingency, Contingency	Planning for the next pandemic. Savings rate increase, balance sheets fortify	Largely business as usual.	Time to build savings. Share buybacks and dividends are delayed. Consumers hold off on discretionary expenses.	Businesses with weak balance sheets are unable to raise debt or equity. Deflation, possible depression, consumers & corps hold off on capital expenditures.	Large cap, well capitalized companies, gold, cash, guns	Venture, Consumer discretionary, Capital intense businesses
Virtual (not) Reality	More virtual vs. face to face interactions. Remote work, medicine, learning, retail, & social	Continued trends with a shift from retail to online, an increase in remote learning, broad social acceptance of "work from home" as an option.	Many retailers go out of business forever. Business travel is diminished. Shared capital declines. Shared labor increases.	Global virtual employment. Borders breakdown as workers compete with global workforce for jobs. Crowded venues & entertainment fall out of favor.	AI, "Cloud services," delivery, global skilled labor, national parks	Bricks & mortar, movie theatres, theme parks, airlines, Airbnb
Urban Flight 2.0	Retreat from urban centers - business and residents go back to the suburbs	Co-working, food halls and micro-apartments fall out of favor. Home prices may decline in high cost centers in West & Northeast.	Shift in preferences towards suburban office and residential. Home prices increase in suburbs and secondary cities.	Urban centers decline. Mass transit falls out of favor. Cities begin investment in driverless car fleets as transit solutions.	Suburban CRE, Secondary sun belt cities	Urban CRE, Municipal bonds, Shared mobility
Enter Big Government	Government as the solution to our social problems. Increased social safety net.	Expectations for government protections against the next Pandemic. Taxes increase, but the existing system holds.	Increasing government involvement in personal health. Taxes increase significantly. Safety net covers healthcare, universal basic income.	Strong border controls. Autocrats and populists use health to hold power. Socialism grows in rich countries. Weak countries fall into chaos. Increased conflict.	Healthcare, Infrastructure, Industry champions, cons. staples	Innovative companies, multi-nationals
Healing Healthcare	Pandemic is the new Cold War. A renewed focus on the cost of healthcare.	Telemedicine is normal. Mental health as a new area of focus. Increased stockpiles of PPE, ventilators, medicine. Hospitals rethink peak capacity.	Hospitals are bailed out/nationalized. Some form of Medicare for all is implemented.	Full European-style, nationalization of the health care system.	Telemedicine, Biotech, Hospital administration, Wearable tech, Psychiatrists.	Health insurance, Doctors, Tobacco