Market Update

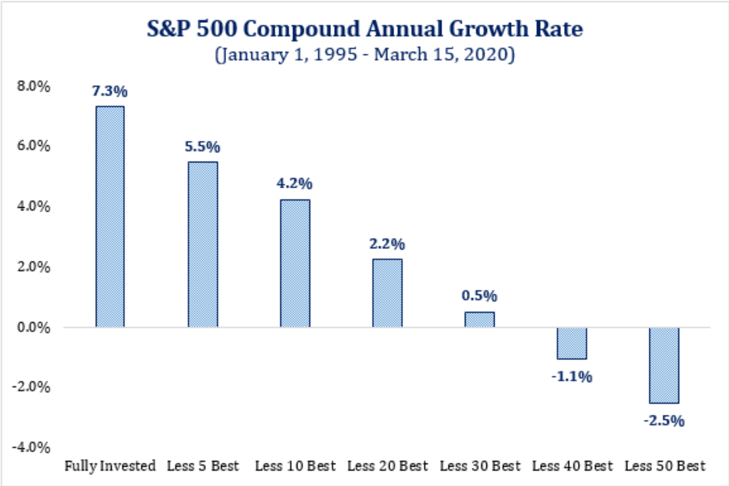
March 20, 2020

First, I want to extend my heartfelt wishes that you, your family, and your friends are safe and healthy, as we struggle to navigate through this challenging period. The virus containment impact on our day-to-day lives has put us in uncharted territory. Stay well.

We will have plenty of time to sort through the long-term economic implications of this global dislocation at a future point. More immediately, in light of the economic and market events over the last few weeks, the US economy will almost certainly suffer a recession in 2020. The severity and duration will be driven by the path of the virus and Washington's response, including recovery stimulus. Over the last week, the Federal Reserve has pulled out nearly all imaginable stops in an attempt to prevent the crisis from having a bigger impact on the financial system, reactivating some financial crisis-era measures. The federal government, through the budget process, appears ready to do the same, and we expect it will be an action-packed weekend as fiscal measures get hashed out. As you likely are aware, Congress is negotiating a shockingly large amount of stimulus. All of these measures will be in place to provide the US economy with ample liquidity while we wait for the virus to be contained.

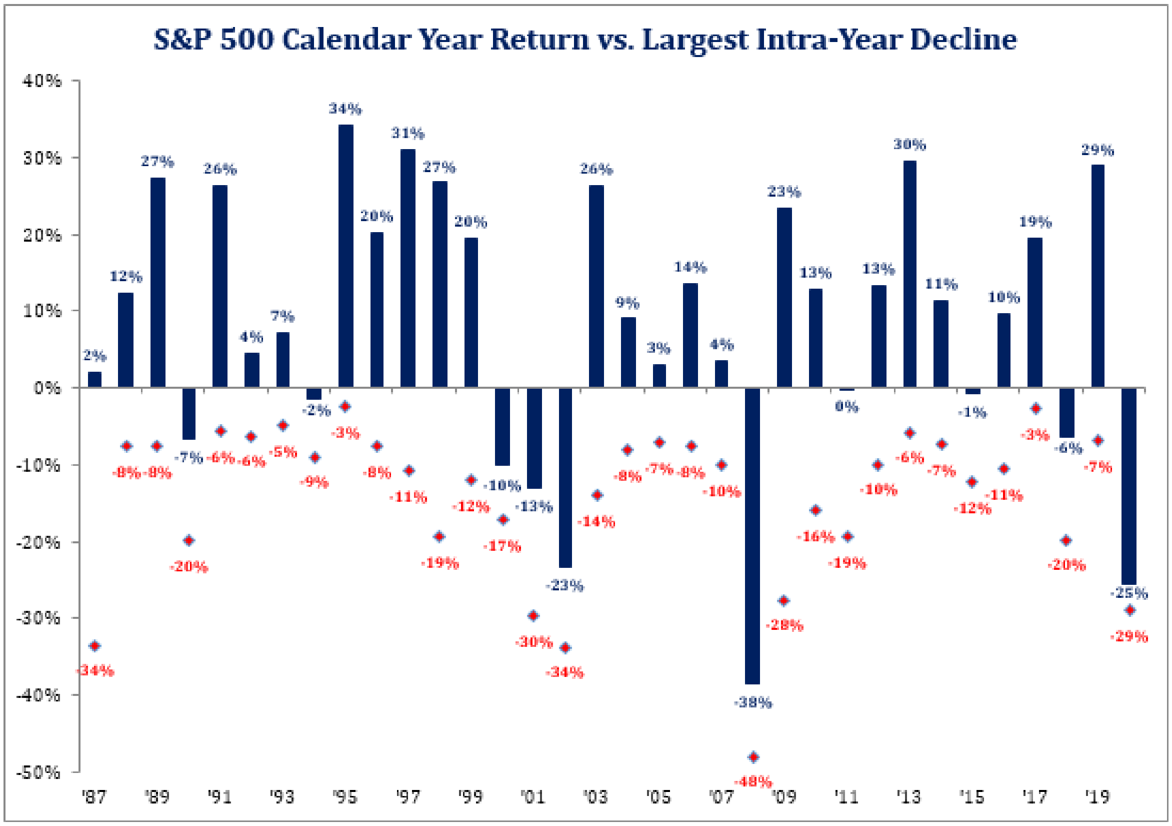
The markets, down 32.1% from the February 19th high, already are pricing in a recession. The most hard-hit areas likely will be travel, leisure and durable goods. There will be some offset to this from higher grocery and healthcare spending. Government spending will mitigate the GDP decline as well. If the infection rate peaks before the economy experiences a deep downturn, both the economy and the markets should rebound quickly (V-shaped), given the health of the economy heading into this crisis and the amount of government stimulus. We still expect a recovery in the second half of 2020 but fully recognize that the longer the shutdown, the deeper the recession.

Looking forward, it may help to remember that the stock market reaches a bottom, on average, four months prior to the end of a recession, with an average gain of 10% in the subsequent six months. In the 6-month window from a market bottom to 2 months after a recession ends, the average market gain is 19.4%. While it may seem tempting to try to time the market, the following chart shows the impact on long-term returns when investors are out of the market on the highest-return days of a year, even when some of those days are within the context of a bear market.



Source: Strategas Research

The measures we are taking are unlike any we have experienced as a nation, at least since World War II. We do, however, have decades of market data to make some sense out of these chaotic markets. Below is a chart that may provide some perspective. Each bar indicates the S&P 500 return for that year. Each red dot shows the largest drawdown within that year. The message is that we have been through markets like this before and, even in good years, there often are big swings.



Source: Strategas Research

Given the uncertainty and timing of the coronavirus cycle, the stock market may suffer additional downside. At the very least, we should expect that the wild swings of late will be with us for the near future as virus headlines continue to dominate every news cycle. In general, market declines end when the cause of the decline is resolved.

Regarding the news, be aware that sometimes the financial "expert" being interviewed has an undisclosed agenda or is looking merely to generate headlines. Likewise, news outlets often are driven by ratings that climb significantly when we are in a crisis. Americans are under enough pressure without the added hysteria.

Finally, here is a small amount of good news. Chinese economic activity began recovering in mid- February as the number of new infections in mainland China has steadily decreased, according to the Webank China Recovery Index, which has risen to 80 from a mid-February low of 23. The Index measures the resumption rate of economic activity in China during the virus outbreak. For example, Apple has reopened all retail stores in China, with most Starbucks and McDonald's stores having reopened as well. The US is not there yet, but we will get there.

If you are looking for a good source of up-to-date global virus statistics, Johns Hopkins has done a good job of tracking the numbers: https://coronavirus.jhu.edu/map.html