Weekly Market Insights

March 9, 2020

Last week the coronavirus, this week an oil spat

The equity markets continued their volatile ride this past week. Interestingly enough, by the end of the week there wasn't a dramatic change.

The Dow was up 1.79%, the S&P 500 up 0.61% and the NADAQ gained 0.10%. The week's ending performance didn't do justice to the price movements between Monday and Friday. During the week, the coronavirus was the principal cause for the flight to quality.

It was not just the equity markets that had dramatic changes. Yields in the credit markets sunk to historic lows.

The Virus

I was fortunate to hear a conference with a number of specialists in contagious diseases. They highlighted some interesting facts that I, at least, was not aware of. The news services have been filled with reports about the spread of the virus. It is indeed true that the virus continues to spread around the globe, but, here are some interesting points. On the discouraging side, there are probably many more cases than have been reported. The reason for this is that most cases are so mild that they are presumed to be a cold, and the victims are not tested for the coronavirus. The flip side of this is a positive. The number of fatalities have been accurately counted, so the published arithmetic telling us the fatality rate is probably well over stated. Having said that, the virus will likely continue to spread. We don't expect a vaccine until early next year, which sounds worse than it really is. The course of the virus, if similar to past viruses, is that it subsides during the summer months.

Another factor influencing the markets, which is related to the virus, is misinformation. Clients should remain cautious to headlines that generate fear. At the moment, our best medical minds believe this is a very contagious virus with a low fatality rate, and most cases will be hardly distinguished from the common cold.

A New Concern

The financial markets must now cope with a crisis in the energy markets. Saudi Arabia and Russia, two major producers of gas and oil, are at each other's throats concerning the price of oil. Saudi Arabia and Russia could not come to an agreement on cutting production of crude. The dispute progressed to the point where the Saudis stopped negotiating and unilaterally lowered the price of oil by about $7.50 a barrel. This was announced on Sunday, and futures markets dropped precipitously. This is just one more unknown for the markets to absorb. This move, of course, hurts the global energy industry, which is a concern for the economy. But, as always, there is a benefit to other parts of the economy. A drop in crude leads to a lowering of prices of gas and other related consumer goods, which leads to higher aggregate demand. Consumer demand in the U.S. is already strong. We don't want to minimize the problems caused by this battle between oil producers, but want to remind readers that there are some offsetting benefits to low energy prices. No one knows when or how the conflict will end, but in our view, it is not likely to be a long term problem.

The Election

Super Tuesday has come and gone, and anyone who is interested has had plenty of time to absorb the shocking result. Biden is now the clear frontrunner and is receiving more and more endorsements, the latest from Kamala Harris of California. Tuesday's primaries may close the door on the Sanders campaign. He, most likely, won't pull out. It's not in his nature, but chances are high that it will be all but over. In all likelihood, this should be a positive for the equity markets.

Where to Now?

Of course, the important question is where does the economy and the markets go from here? We continue to believe the U.S. economy is strong enough to withstand the assaults from both the coronavirus and the battle between the Saudis and Russians. The consumer remains strong, lower oil prices help demand, and supply chains will gradually reform. The historic drop in interest rates will also boost consumer spending. If our assumptions about the U.S. economy are correct, then the equity markets will come back and likely reach new highs.

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