Flash Market Commentary

Since we published our most recent Flash Market Commentary on February 26, we have continued to see significant volatility in both the equity and fixed income markets, despite the Federal Reserve enacting an inter-meeting .50% rate cut and the Democratic Presidential primary process taking what many would see as possibly a more market friendly turn. This would include Monday (3/9) when stock market circuit breakers went into effect for the first time in over two decades. In addition to recent issues in regard to the price of oil, the primary culprit has continued to be the coronavirus, a topic which has produced a highly divergent range of opinions, even among medical professionals, from "media driven hysteria over nothing" to "unprecedented, unstoppable epidemic".

Regardless of who will eventually end up being correct, typically somewhere in the middle, we are currently experiencing an adverse feedback loop where one piece of potentially negative news builds upon itself in a domino like fashion. The concern is that this will negatively impact consumer sentiment, which has been the foundation of the U.S. economy comprising approximately 70% of U.S. GDP. A precipitous fall in consumer confidence could transition a "supply chain shock" scenario, tending to have a relatively quick recovery as pent up demand results in a bounce back in manufacturing, to a "demand shock", which could be a more elongated process to unwind due to the fact that services per se (travel, conventions, concerts, etc.) don't necessarily come back. The psychological element of school closures, although hopefully short-term, should also be a consideration. This all adds up to a potential "paradox of containment", where strong virus containment efforts could lead to a significant short-term economic disruption, and a further reduction in 2020 earnings expectations, while presumably mitigating the potential longer-term impacts.

As one would imagine, given the sparse and fluid flow of concrete data, modeling this type of scenario is difficult, but among other items, we are currently digesting the following:

- The growth rate of the coronavirus in China has slowed considerably to less than 1% daily. As of Friday, March 6, the number of cases totaled just shy of 81,000, with over 3,000 deaths and nearly 54,000 full recoveries.

- Albeit having somewhat different dynamics than the U.S. financial markets, the Chinese equity market has already seemed to have stabilized over the last month.

- Outside of China, the daily growth rate has been in excess of 15%, up to 24%, with the total number of cases reaching the 20,000 level with 368 deaths and over 2,000 full recoveries to date.

- Bond prices have surged as interest rates have materially fallen. For example, the 10-Year U.S. Treasury, which is an important component in determining mortgage rates, has fallen from 1.92% at the end of 2019 to .58% currently. In essence, bonds have once again proven to be an excellent ballast against equity volatility.

- Since the end of 2019, oil prices have declined significantly (almost 50%) due not only to coronavirus related global recession concerns, but also the lack of an OPEC/Russia deal on production cuts. With the events over the weekend, this situation shows no signs of stabilizing any time soon. Although negative news for the energy patch may become a stimulus for consumers and certain industries, given the debt levels of many oil related companies, lower prices may add strain to their balance sheets, resulting in a decline in capital spending.

- As evidenced by the moves last week, central banks across the globe seem committed and poised to take whatever monetary actions they deem appropriate to combat economic headwinds. Discussions in regard to potential global fiscal stimulus and liquidity, among other possible levers, are underway as well.

At this point, there are certainly a variety of unknowns, including whether or not this health situation actually does turn into a true pandemic or epidemic. And, it is impossible to accurately predict the turning point of the economy or financial markets. However, as we have alluded to previously, situations similar to this have historically been transitory, playing out over a three to six month period. We continue to keep abreast of numerous aspects in regard to this situation and certainly hope history will be repeated, not only from a financial perspective, but also a human one as well. We will be keeping particular attention on developments within the energy sector as well. In the meantime, although certainly not a guarantee, we should all remain aware that "panic selling" historically has been a recipe for underperformance as some of the stock market's best days have followed its worst. Yet another reason to have a long-term focus.

As always, please don't hesitate to contact your Portfolio Manager with any questions or concerns.

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