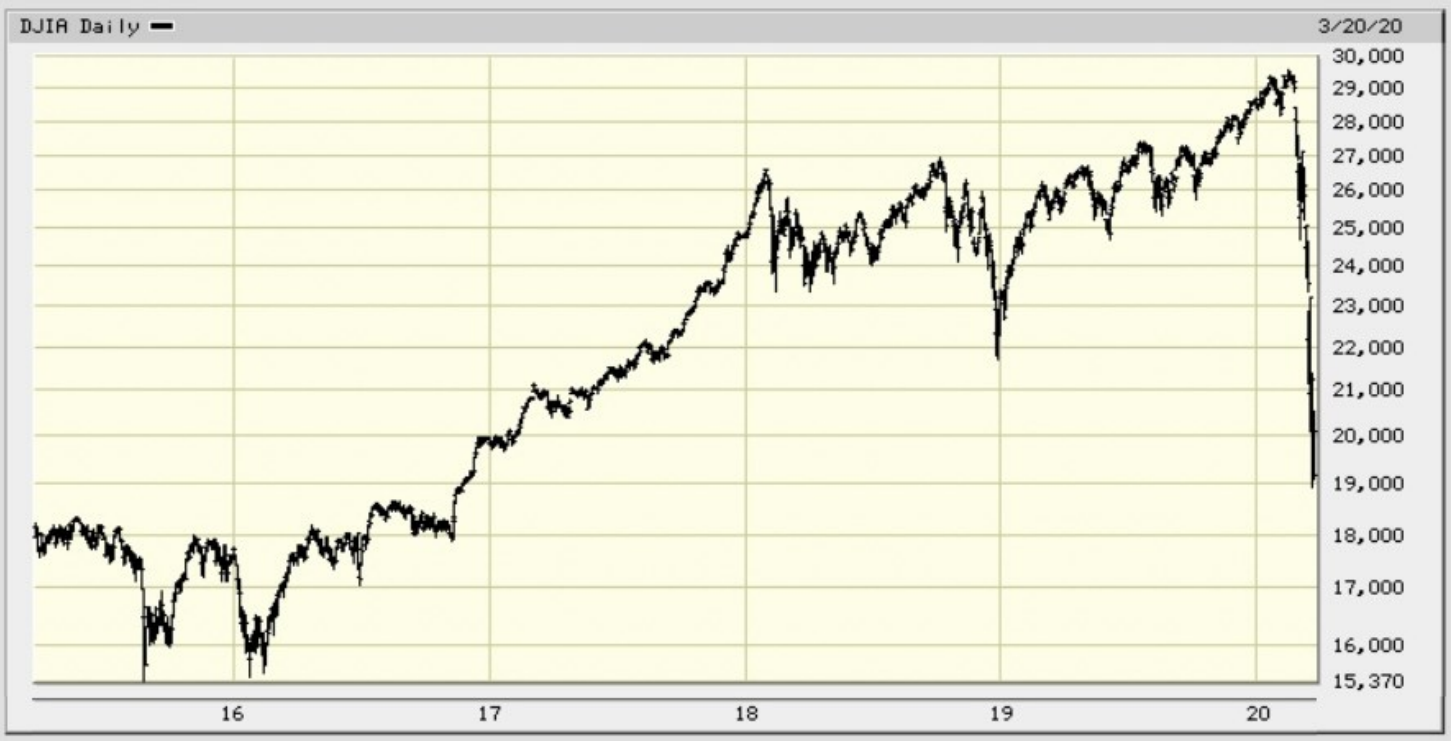
Chart of the Month

March 2020

SPECIAL WEEKEND EDITION



The world is at war with an invisible enemy. The coronavirus has quickly turned a health crisis into an economic crisis. In our efforts to contain the former, we have exacerbated the latter with government "stay at home" directives and non-exempt business closures. The economy is all but officially in recession now and the question is no longer if but how long and deep the downturn will be.

The good news is that the extreme measures already implemented should slow the progression of contagions in the weeks ahead (even though the reported number of new cases will suggest otherwise due to an expansion in testing). The bad news is that the financial toll is likely to accelerate at least through the spring with employees losing jobs and employers losing revenue.

As for the stock market, the Dow Jones Industrial Average plunged 17% in the most volatile week ever and has now fallen 35% from its peak a month ago. While the Dow has declined more than 10,000 points in a matter of weeks, it is still higher than at any time prior to late 2016. In other words, stocks have given back about 3-1/3 years worth of gains. Dividends (which are not included in the index's value) have mitigated part of the fall. At an average annualized yield of approximately 2%, the DJIA has produced a cumulative return of roughly 7% during this period. Not a great outcome but certainly not the end of the world either.

Our intention is not to be dismissive of the recent carnage but instead to add perspective at a time when confusion and uncertainty reign. We recognize that it is disheartening to see the market value of one's portfolio drop, particularly as precipitously as has been the case over the past 30 days.

Where do we go from here? The answer is nobody really knows. We are in uncharted waters. The massive amount of monetary and fiscal stimulus will help reliquefy the financial system in time but neither will solve the pandemic itself. Only new vaccines and therapeutics — and perhaps warmer weather — will do the trick. In the meantime, we can all do our part by sanitizing regularly, practicing social distancing, getting lots of sleep, eating healthy, exercising, and staying in touch with family and friends.

What we should do next is as much a personal decision as it is an investment decision. One size does not fit all. The course of action is a function of each client's risk tolerance and time horizon. For those who have a longer-term outlook coupled with the patience, financial wherewithal, and ability to weather the storm, then staying the course (while making strategic changes along the way) is probably the best solution. On the other hand, those with a shorter-term outlook and/or the inability to see it through, then raising cash by reducing or eliminating stocks (and perhaps other assets) is the sensible alternative.

For clients who no longer wish to risk their principal, government securities are the way to go. Their safety, however, comes at a price with negative yields on three-month and six-month Treasury bills and negligible yields for 12 months (0.08%), two years (0.31%), five years (0.46%) and ten years (0.85%).

The nastiest of the bear markets in most of our lifetimes (1973-74, 2000-02, and 2007-09) have averaged peak-to-trough declines of 45-50%. A similar contraction this time around would suggest that the Dow could drop to about 15,000-16,000 or another 15-20% before bottoming. The decline in a more normal bear market (if there is such a thing) has ranged between 25-35%. Either way, the rebounds have typically been fast and furious. From the low in 2009, the Dow climbed approximately 35% in three months, 45% in six months, 55% in nine months, and was up nearly 65% a year later.

While the news will certainly worsen before it gets better, the stock market is a discounting mechanism and generally leads on the way down as well as on the way up. As such, the market *may* be closer to its nadir in terms of both time and price. Remember, it is always darkest before the dawn. The extreme levels of panic, despair, and capitulation will be most evident at the bottom. Are we there now? Maybe but probably not quite yet.

Although the decline in the prices of stocks has been dominating the headlines, the values of risk-based assets have declined virtually across the board. Corporate bonds have been negatively impacted by credit concerns and a sudden lack of demand. Real estate is not immune from the vagaries of the economy and has undoubtedly been adversely affected by the same variables as stocks. The difference is that stocks are priced in real time and arguably too liquid for their own good while real estate is illiquid and not priced on a moment-by-moment basis. As such, real estate investors are sometimes blind to the changes in market value and neither in tune with the peaks nor valleys of these unpriced assets.

In the short run, stocks bear the brunt of the damage because they *can* be sold and turned into cash easily with the difference in trade and settlement dates a mere two business days. Real estate, when listed for sale, is generally on the market for weeks, if not months, and subject to a 30- or 60-day escrow with commissions and other closing costs of at least 5% in most cases.

We can't control everything that happens to us in life, but we can control how we react to these events. With the foregoing in mind, we encourage clients to let us know whether they wish to stay the course or make changes to the asset allocation and/or types of stocks in their portfolio(s).

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