Market Comment: Coronavirus March 2, 2020

The coronavirus went global last week impacting multiple continents. Fear over the impact of the pandemic caused investors to sell stocks indiscriminately. The S&P 500 declined 11.49% last week and 12.26% below its all time high on Feb 19 while investors bought scads of treasury bonds for safety causing their prices to rise.

The market despises uncertainty. There have been several guesses at how much impact the virus will have on the global economy due to impact on business operations and productivity in China Supply chains are disrupted and the delay (impact) products getting to market. This disruption will have a direct impact on gross domestic product (GDP). Original estimates were for 2% GDP growth in 2020. Now GDP growth may be 1% or lower. Stock prices are driven by corporate earnings. 2019 earnings were up 3.64% and 2020 earnings were projected to be up 5%. We now expect 2020 earnings will be flat.

As we highlighted in our January market commentary, we have been anticipating increased volatility and the possibility of a correction that no one would see coming. This is it.

Should the spread of the coronavirus be contained in the short term, we believe fundamentals will remain intact. Economic factors did not start the selloff in the market. Fear over the impact of the coronavirus caused the selloff. This is why we think this will be a short term. Afterwards there will be pent up demand and likely a flurry of activity to bring the economy back into balance. Sometimes no action is the best action. We suspect that any drop in earnings or economic activity will be short lived, and more than made up for in the year to come.

We have invested your portfolio to withstand this very shock. We set a strategic asset allocation based on your personal situation, considering your time horizon, risk tolerance, and goals. For more aggressive portfolios you have less in cash and bonds because your risk tolerance is higher and you have a longer time horizon. Short term selling or market timing rarely pays off. For more moderate portfolios with 40% +- in fixed income and cash, the impact on your portfolios will be much less than the overall market. We are seeing our moderate portfolios down about 5% vs the S&P 500 down 11% YTD.

We actively monitor your asset allocation. If your allocation to bonds becomes too large, we will reallocate back into equities. For example, if we have your portfolio set to a 60% equity 40% bond mix and bonds are now 50% of your portfolio, we will move 10% out of bonds and back into equities to bring you back to your target allocation.

When the market sells off for reasons other than fundamental or economic it is very helpful to look at price charts to see if we should expect more selling and if so, how much. Price charts or technical analysis ignore the emotion that can drive stock prices and measures pure supply and demand for stocks. The run in the S&P 500 from Jan 2019 to Feb 2020 has been cut in half or the price has retraced 50% of its run during that period. This is an important technical level and can indicate the selling is getting close to the end.

The number of stocks trading above their 200 day moving average (MA) is another technical indicator that measures momentum or how strong prices are moving up or down. December 2018 saw only 16% of stocks trading above their 200 day MA after a 20% price decline in the S&P 500 in the 4th quarter. February 2020 ended with 27% of stocks trading above their 200 day MA. The range has been as low as 14% in September 2011 to a high of 78% in July 2013. Since then the percentage of stocks trading above their 200 day MA has maxed out closer to 70% of stocks. The range since 2014 to today has been 20%-70%. This indicator suggests we are closer to decent entry point with more limited downside risk.

The Fear & Greed index is at 11 which indicates Extreme Fear levels. This is down from Extreme Greed levels in late 2019 and early 2020 when readings were in the high 90s. In late 2018 there were multiple readings in the Extreme Fear range due to Powell, the Fed, raising rates. Today there is no risk of rising rates but much hope for rate cuts this year (as of this morning, the Fed announced a surprise 50 basis point rate cut). We expect central banks around the world to err on the side of more accommodation until the impact of the virus can be better quantified.

Moments of heightened anxiety and market volatility tend to induce greater emotion. There is an inclination for investors to want to take action, when in reality, doing nothing might be the best course of action. We believe this is the case right now. While we believe the coronavirus will ultimately prove to have a short term impact, the truth of the matter is we cannot say for certain based on the data that is currently available. We do, however, continue to feel strongly that staying the course over the long run is the most prudent way to invest successfully. Risks to the market always exist whether they are in the news or not. As your advisor, it is our job to make sure you have a plan in place for times exactly like this; to anticipate and not just react, while also being flexible. After 30 years, we have witnessed many market events and none are exactly the same. If you have any questions, please do not hesitate to contact us with your concerns. In the meantime, know that we are paying attention and monitoring all developments closely, and we will continue to keep you posted as conditions warrant.