Assessing the first four months of 2020

Where we go from here

The last several months saw a tremendous shakeup of both the global economy and capital markets as the COVID-19 pandemic spread worldwide. This resulted in significant challenges for investors, consumers, businesses and governments at all levels. It can be helpful to gain some perspective by taking a look back at the major events we’ve experienced. In addition, we consider what’s to come as we move forward through the rest of 2020 and beyond.

A swift capital market reaction

From the day the Wuhan Municipal Health Commission in China reported the first cluster of pneumonia cases in Hubei Province (December 31, 2019) through the present day, we’ve witnessed some dramatic changes.¹ These stunning developments had significant ramifications across asset classes and geographies. U.S. stocks, as measured by the S&P 500, reached their all-time high on February 19 before falling more than 30% within the next 23 trading days. The uncertainty surrounding the health crisis cascaded into indiscriminate selling across stocks, bonds, currencies and commodities. This provided a stern test for investors’ mettle, as they coped with a seemingly 24/7 news cycle of COVID-19 headlines and the resulting impact on their loved ones, acquaintances and livelihoods.

In addition to the sharp reaction in consumer and business demand-sensitive categories like stocks and real estate, the energy market faced unique challenges. While slower economic growth adversely affects oil prices, on March 6, delegates to an Organization of the Petroleum Exporting Countries (OPEC) conference in Vienna, Austria, failed to agree on output cuts intended to solidify oil prices. The subsequent rout in oil prices introduced a new shock for investors and companies within the energy complex.

The one-two punch of COVID-19 uncertainty and energy market gyrations drove asset prices lower. The market reaction included several days of difficult trading where buyers and sellers faced very illiquid markets. In such an environment, buyers and sellers are far apart and prices reflected considerable selling pressure. Investors awaited clarity on policy measures and a read on the full economic impact of the virus. Even with declining asset prices, many investors were content to sell first and seek the perceived safety of cash and safer components of the bond market.


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[ 1 ] Important disclosures provided on page 5.
After reaching a low point in late March, stock markets recovered some of their losses, but the environment remains volatile.

**A period of unprecedented government and central bank intervention**

The rapid spread of COVID-19 forced the implementation of policies that effectively shut down wide swaths of the global economy. In the U.S., this led to the sudden layoff of tens of millions of workers and the likelihood that the U.S. economy has been driven into a deep recession. The virtual economic shutdown is considered the primary strategy to “flatten the curve” of the coronavirus. Therefore, the federal government and Federal Reserve Bank stepped in to try to provide financial support to limit the economic damage. The steps they took occurred more quickly and involved a far larger financial commitment than at any other time in history.

**Federal government actions**

Congress and the Trump administration came together to enact four different stimulus packages. In a matter of weeks, four major stimulus packages valued at more than $2.5 trillion were implemented. The major provisions of these packages include:

- A one-time payment of up to $1,200 per adult and $500 per child under age 17 (subject to income limitations)
- The Paycheck Protection Program, offering loans for smaller-to-mid-sized businesses designed to help them keep individuals employed
- Expanded unemployment benefits of up to $600 per week for qualified individuals who are collecting state unemployment checks
- The ability of independent contractors, gig workers and freelancers to collect unemployment benefits
- Deferral of up to six months of mortgage payments for some mortgage holders
- The suspension of payments for federal student loans until September 30, 2020
- The flexibility for those under age 59-1/2 to take penalty-free distributions of up to $100,000 from workplace retirement plans and IRAs, with taxes spread out over three years but potentially waived if the distributed funds are replaced
- A one-year reprieve from IRA and workplace plan required minimum distributions for 2020

In addition, the federal government pushed the tax-filing deadline from the standard April 15 to July 15. Most states followed suit. Be sure to check with your tax advisor on how specific rules relate to your circumstances.

An executive branch measure invoked by President Trump was the Defense Production Act. This was put into place to impose requirements on certain firms to produce much-needed medical supplies and to keep meat-processing plants operating.
**Federal Reserve actions**

The Federal Reserve was also active during this period of economic uncertainty, seeking to intervene where it could to help stabilize the economy. Among the steps implemented by the Fed were:

- Reducing the Fed Funds rate it controls from the 1.5% to 1.75% level as it stood in early March to a 0% to 0.25% target range

- Restarting its quantitative easing program, purchasing trillions of dollars-worth of fixed income securities to help keep those markets liquid

- Allowing the ability to leverage $450 billion included in the government stimulus package for businesses to extend up to $4 trillion in loans

- Making an additional $2.3 trillion in loans available for a variety of purposes, including providing capital to small- and mid-sized businesses with up to 10,000 workers and revenues of less than $2.5 billion

It is likely that additional federal government and central bank stimulus will be forthcoming as needed to continue to cushion the economic impact of the social distancing measures associated with COVID-19 as states and businesses slowly begin to bring the economy back online. Even with this substantial intervention, the U.S. economy (as measured by gross domestic product) declined by 4.8% (annualized) in the first quarter.

**Outlook**

While most markets remain below their all-time highs and are down for the year, we have seen a meaningful snapback following the (hopeful) crescendo in stocks and other traditionally risky asset classes. Energy prices, specifically oil, have been an exception, with supply and demand imbalances maintaining downward pressure. Aside from ongoing troubles in the oil patch, the S&P 500 shifted gears quickly. It experienced the fastest bear market drop in history (defined as a 20% decline) from all-time highs, to the fastest bull market rally out of a bear market in history (defined as a 20% gain). What does this unprecedented asset price volatility mean for investors, especially in light of looming economic challenges?

Markets are forward-discounting mechanisms, meaning today’s prices anticipate future outcomes. Prices on February 19, when the S&P 500 was at all-time highs, anticipated a global economy still growing and consumers and businesses continuing to enjoy the benefits of a long-standing economic recovery. When stocks dropped to their low point of the year on March 23, investors envisioned a world with impaired consumer and business activity as forced shutdowns persisted around the globe. At time of this writing, global stock markets are about halfway between their February all-time highs and their March nadir. We have dubbed the current economic state as the “muddle through” stage, characterized by progress in thwarting the virus’s spread, significant stimulus from policy makers, gradual economic reopening, but uncertainty about how long the global economy will operate so far below its potential. The more gradual the recovery, the deeper the economic pain, and vice versa. We remain long-term believers in the power of human ingenuity and the global economy’s ability to drive towards homeostasis, or the self-repair that occurs over time. The path ahead will likely occur in fits and starts, with setbacks and advances that are far more consequential than dollars and cents. Nevertheless, we expect that patient investors may be rewarded for the risks they take within a diversified portfolio appropriate for their unique situation.
Make sure you are prepared

We are living in a time of significant uncertainty with events occurring that could potentially alter your own plans. This may be an opportune time to assess how your financial plan and your portfolio have been affected by the events that have occurred thus far. You want to ensure that your investments are appropriately positioned given today’s challenging market and economic environment and for the opportunities that lie ahead. Speak with your wealth management professional about reviewing your financial plan to help you stay on track as you pursue your goals.
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