FCI ADVISORS

CAPITAL MARKET COMMENTARY

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An Unavoidable Consequence of Flattening the Curve

Our nation and the world are fighting a virus the likes of which we have not seen before. While America has had its share of fights with nasty enemies in the past decades and centuries, this enemy is a different type of foe. It is a virus that is impacting the entire globe. It is invisible. It is rapidly moving.

The world has realized much more fully in the last week the only way to beat this foe, which we will do, is to distance ourselves from one another. We are confident the world, and Americans in particular, will rise to the challenge. As perverse as it sounds, we will come together to defeat this foe by being more physically apart.

This distancing is the key to "flattening the curve," an expression that speaks to curtailing the spread of this nemesis. Social distancing will work. It is a proven way to slow the virus. China has proven that in the last few weeks. However, an unavoidable consequence of the social separation is a virtual freezing, albeit temporary, of the economy. To ward off the virus, we are anticipating the economy will be brought to a temporary halt.

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How Temporary is Temporary?

The markets are struggling to answer that question right now. The equity market in the U.S. has now experienced the fastest decline from a peak level to bear market territory in its history. It happened in just 16 trading days. Capital markets are attempting to figure out the breadth and depth of the economic chill. However, that cannot be determined with any accuracy until we have a better read on the virus curve. There is no precedent for this situation, particularly in the type of global society we have today, one that is so physically mobile and technologically interconnected. Therefore, the markets want to see progress in flattening the curve. The capital markets are responding more favorably to the steps being taken to slow the spread of the virus than the interest rate cuts by the Federal Reserve. The Fed cut rates by a total of 150 basis points last Wednesday and Sunday. Stock markets fell dramatically the day after each cut. When stock markets received better news on the planning and preparation for slowing the virus last Friday, they rose.

Congress is also in the midst of finalizing several fiscal policy moves. While these moves may not prevent the economy from having two quarters of negative GDP growth, the definition of a recession, they should minimize some of the downside. They should also make it easier for the economy to recover once the virus has been minimized. China has shown that following containment and quarantine, the economy can begin to recover. While Apple is presently closing its stores in the U.S. for the next several weeks, it is now in the process of reopening its stores in China. The American consumer has been a stalwart for the economy, and lower interest rates for longer should continue to benefit the consumer. The Fed and Washington are doing all they can to insure there is ample liquidity.

Resist Temptation

Until the social distancing being practiced begins to foster a slowing of the contagion, markets are going to be volatile. The S&P 500 is now down 26% in only 19 trading days from the all-time high on February 19. A move of this magnitude typically would take 4 to 5 months, on average. Large swings tempt investors to make dramatic moves themselves. We advocate resisting that temptation. Nobody knows the exact moment when better containment of the virus will be evident. However, the market will react immediately at the first hint of improvement. In fact, the markets will likely anticipate a turn and move even before the improved numbers appear. Markets always have and always will be discounting mechanisms that constantly look ahead. In our opinion, the ensuing upside move, though we don't know exactly when it will occur or from what level, will be powerful.

What to do?

In capital markets that are as volatile as any we have seen since 2008 and 1987, we are preaching the virtues of four words: Patience. Balance. Self-control. Courage. It is important to keep emotion from dominating the investment decision-making process. Our markets have proven over the years to be very resilient and we expect them to be again. We are counseling clients to recognize these market realities, keep clear objectives in mind and stay the course that is best for them. We are here to serve. Remember that the United States of America is a resilient nation. We have ingenuity, resolve and industriousness on our side. When Americans are being asked to unite against a common foe, we have always risen above our differences and overcome our foes. This foe is of a different nature and because of that nature the time necessary to overcome it is uncertain, but we will prevail.

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As always, please contact your portfolio manager with any questions.

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