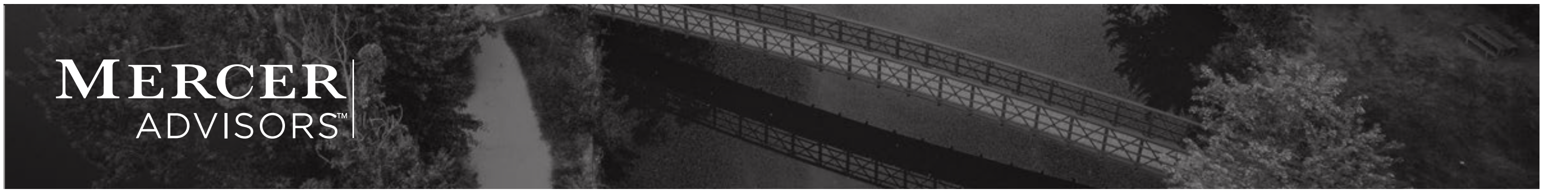

Tuesday, March 10, 2020

MONDAY'S MARKET DECLINE

Over the weekend, Saudi Arabia shocked the world with a surprise announcement that they would cut the price of oil and significantly increase production. This decision came after OPEC talks collapsed on Friday when the cartel's major players, Saudi Arabia and Russia, disagreed on price and production targets. This announcement comes on the heels of recent market volatility, the continued spread of the COVID-19 virus in the United States, and Italy's decision to quarantine large parts of the country in an attempt to stem the virus' spread.

MARKET REACTION

Oil prices collapsed nearly 30% on the news; the yield on the 10-year US Treasury bond hit an all-time low of 0.32%; and US equity markets reacted to the news by opening down nearly 7% from Friday's close. The NYSE's circuit breakers kicked in to temporarily halt trading. For those unfamiliar with circuit breakers, they are regulatory tools used to calm markets when markets decline more than 7%. It's a trading curb that temporarily halts trading for 15 minutes; in extreme cases, such as a greater than 20% decline in market prices, trading would be halted for the remainder of the day.

MARKET CLOSE

The S&P 500 Index finished the day down 225.81 points or -7.6%; the Dow Jones had its largest point loss in history and its 11th largest percentage loss. Non-US markets are down in a similar range. US bonds yields hit all-time lows with the yield on the 10-Year US Treasury bond closing at 0.559% after hitting an intraday low of 0.318% earlier in the day.

WHAT WE KNOW AND WHAT WE DON'T KNOW

Oil Prices

We don't know if this is a permanent policy commitment by the Saudis or if this is gamesmanship to force the other OPEC nations, especially Russia, to the negotiating table. We do know that oil prices at this level are likely to take a significant number of US rigs out of production and will likely hit employment in the US energy sector particularly hard. We also know that if low oil prices persist, US consumers will benefit from low prices at the pump.

The Coronavirus

We don't know the ultimate impact the COVID-19 virus will have on the American people, nor do we know exactly how it will impact the US or global economy, but we can make an educated guess. We know that human civilization today is more prepared than at any time in our history to contain, treat, and ultimately cure diseases caused by the virus. In time, we will learn to manage and live with this virus, much like we have others. We know that the infection rate in China appears to be leveling off. We know too that the fatality rate (relative to confirmed infections) is approximately 3%; it's likely much lower given the (likely) large number of asymptomatic carriers (those who carry the virus but don't become ill).

The US Economy

We can surmise the US economy may be heading into a recession, at least in the short run. As demand declines due to the spread of the coronavirus, corporate profits will decline. The US energy sector will shrink as a result of lower oil prices. This will likely depress stock prices, especially in the energy sector, over the short-term. But longer-term, the US economy will recover and be fine. US consumers will benefit from lower prices at the pump and lower interest rates, both of which should help buoy long-term economic growth.

Financial Markets

We don't know how long the current market correction will last or if the worst of it is behind us. We do know that market corrections are not new and they're certainly not rare. Since 1928, the US equity market has experienced 53 corrections (10% declines) or bear markets (20% declines), about one every 18-24 months. The last time we saw a similar correction? The fourth quarter of 2018. The market declined nearly 20% from its high in September 2018 and hit bottom on December 24, 2018. What about before that? Before that we had corrections (going back in time) in 2016, 2015, 2012, 2011, 2009, 2008 and so on. Yet we're still here and the market has continuously recovered and gone on to post new highs. This market correction too shall pass.

FOCUS ON WHAT YOU CAN CONTROL

We should focus on what we can control. We can't control markets. Markets experience corrections from time to time—that has been true since the dawn of history. But while we can't control markets, we can control how you respond to bad markets. We should remain calm. If watching the evening news gets us worried, we should avoid it. Likewise, let's avoid the blogosphere and social media if they're doing to get us upset. If you're worried about the future state of the economy and how it might impact your household finances, you might consider delaying large purchases or other planned expenses.

WE'VE PLANNED FOR THIS

It's important to remember that your financial plan and advisor have planned for this day. This is why you're in a globally diversified portfolio. It's why your portfolio should continue to hold bonds, even when rates are low. It's why you meet quarterly with your advisor to review and update your plan. This is also why we systematically and periodically rebalance your portfolio. Rebalancing ensures your portfolio "buys low and sells high", that it remains on target over time, and that is remains aligned with your risk tolerance. My point? Your financial plan was constructed on the very expectation that markets would experience deep corrections in the future, not the wishful thinking that markets would continue to go in a straight line forever. That seems obvious, but it bears reiterating; expert, high quality financial planning requires that we plan for future market volatility.

GOING FORWARD

Market corrections are a fact of life. They won't go away and timing them is futile. But there are some good things about bad markets. Market corrections allow investors to benefit from dollar cost average and rebalancing. Declining interest rates present opportunities to refinance an existing home or to buy a new one. In the tax planning arena, clients might consider working with their advisor to explore a Roth IRA conversion or harvesting tax losses. It's relatively easier for clients with low basis taxable investments to diversify those investments. My point is that market volatility comes and goes; we should expect and accept it. We should accept market volatility for what it is—a fact of life, yes, but importantly, also a planning opportunity with the help of a trusted, expert advisor. After all, that's why we're here and why we're honored to continue to serve you and your family.

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