March 27, 2020

## What Happened in the Markets?

- US stocks fell sharply on Friday as the S&P 500 declined 3.4% to close at 2,541. With the sell-off, the index is now down 21.3% year to date and has corrected 25% from the February 19 all-time high.
- Even with Friday's losses, the S&P 500 still posted its strongest week in more than 10 years as markets reacted to a flurry of action from policy makers. The week ends with a signing ceremony at the White House for the $2 trillion stimulus package that sailed through the House earlier on Friday after previously being passed by the Senate on Wednesday. These stimulus measures should help provide a bridge to an economy dealing with the "sudden stop" brought about by the virus and associated response.
- Ten of the 11 S&P 500 sectors were lower Friday, with Utilities (+0.5%) and Real Estate (-0.1%) outperforming the broader market, while Information Technology (-4.6%) and Energy (-6.9%) lagged.
- Rates were lower across the curve, with the yield on the 10-year falling to 0.69% as of the 4 p.m. equity close. The yield curve flattened, as 10-year rates fell more than 2-year rates. WTI oil fell 4.2% on the day, and is currently under $22 per barrel, while gold declined modestly; the US dollar moved slight lower—its 5th day in a row trading lower—as measured by the US Dollar Index.

## Catalysts for Market Move

Stocks limped into the weekend Friday, with the S&P 500 off 3.4%, to close at 2,541. There were no clear catalysts for Friday's decline, but some consolidation of the week's gains may have been due following a ~20% rally in the major averages from Monday's lows to Thursday's highs. Even with Friday's pullback, it was still a historic week for US equities, as the 10%+ gain from last Friday's close marks the strongest weekly performance for the S&P 500 since the rally off of the trough in March 2009. This week's strength comes in stark contrast to last week's slide, in which the S&P 500 shed 15% in its worst week since 2008. Optimism has crept back into markets this week as policy makers have moved decisively to address the economic issues at hand as a result of the spread of the coronavirus and associated response.

The week began with the Federal Reserve unleashing a number of measures designed to stabilize fixed income markets and ensure liquidity flows through the financial system, and the week ends with lawmakers following through with a $2 trillion stimulus package aimed at providing relief to those individuals, businesses and organizations most affected by the "sudden stop" in economic activity caused by the spread of the coronavirus. The newly enacted Coronavirus Aid, Relief and Economic Security (CARES) Act, was passed by the House of Representatives Friday afternoon, and signed into law by the president just after the close of trading on Friday. The CARES Act includes support in the form of loans and assistance for large companies, small and medium-sized businesses, states and local governments, and hospitals. On the individual side, the bill provides for direct payments to lower- and middle-income individuals and families, and expands unemployment insurance benefits.

Markets have been watching policy makers closely in recent weeks for signs of action, as it becomes clearer that the economy will take a near-term hit as a result of the disruption associated with the spread of the coronavirus. More nations and regions have moved toward limiting cross-border traffic and encouraging 'social distancing' within their borders, with much of the US and Europe now subject to some type of recommended lockdown. Ultimately, these efforts should help address what is first and foremost a public health concern, but clearly the economic disruption from the virus will be felt in the near term as these containment efforts disrupt businesses and working life. An early gauge of how disruptive the virus could be for the economy was seen in Thursday's weekly jobless claims report from the Department of Labor. The report showed a record 3.3 million Americans filed for unemployment benefits for the first time last week. This sharp increase in unemployment is likely a result of the "sudden stop" impact the virus/virus response has had on the economy, and underscores the need for fiscal stimulus on the scale that will be provided now that the CARES Act has been enacted.

While this week's gains are welcomed, the recent pickup in volatility remains unsettling. Investors should be prepared for the market to remain volatile in the coming weeks, particularly given the nature of the current market sell-off, which has been driven, in part, by anxiety over the unknown as it relates to the spread of the coronavirus. To that end, the market is pricing in volatility to remain extraordinarily high, as measured by the CBOE Volatility Index, or the VIX. The VIX tested its 2008 Financial Crisis highs last week trading above 80, but has since fallen toward the mid-60s this week; while the VIX has come down from last week's high, current levels still imply a ~4% daily average move for the S&P 500 over the next 30 days. From a relative valuation standpoint, equity earnings and dividend yields also look attractive when compared to long-term Treasury rates, suggesting the market has priced in substantial risk, and opportunities may be presenting themselves for long-term oriented investors.

## The Global Investment Committee's Outlook

The dual shocks of coronavirus and the collapse of OPEC-plus, causing oil prices to fall dramatically, are likely to push the global economy into recession over the next 2-3 quarters, ending the 11-year business cycle. However, the swift and furious bear market sell-off since the S&P 500 all-time high on February 19 leaves most asset classes already fully discounting that outcome. Furthermore, we are anticipating an increasingly coordinated "do whatever it takes" stance from global policymakers who are likely to deliver both monetary and fiscal stimulus that should stabilize things as we navigate the human disruption and health-related parts of the crisis. On the other side of the recession, we see potential for a V-shaped global recovery. Green shoots were already visible outside the US, and inside the US, the foundational health of the consumer has never been stronger to weather a recession, i.e., low unemployment, strong balance sheets and housing market with momentum. Consequently, on March 13, the GIC reduced exposures to long-duration Treasuries and began rebuilding exposure to US large-cap growth, US small/mid-cap stocks, and high-quality investment grade credits that are benchmarked to the Bloomberg Barclays US Aggregate. While we believe the current equity market correction constitutes a cyclical bear market within a longer-term equity bull market, the GIC believes a new multi-year bear market in fixed income has begun.

The next leg of the secular bull market in equities is unlikely to see the same leaders as the past decade—namely Technology and Consumer Discretionary stocks. Instead, the GIC sees Financials, Industrials and Healthcare stocks likely to outperform. Volatility over the next few quarters should be exploited frequently to rebalance portfolios to strategic asset allocations.

Market data provided by Bloomberg.
**Dow Jones Industrial Average (DJIA):** A price-weighted average of 30 blue-chip stocks that are generally the leaders in their industry.
**NASDAQ Composite Index:** A broad-based capitalization-weighted index of stocks in all three NASDAQ tiers: Global Select, Global Market and Capital Market.
**S&P 500 Index:** The Standard & Poor's (S&P) 500 Index tracks the performance of 500 widely held, large-capitalization US stocks.
**US Trade-Weighted Dollar Index:** A weighted average of the foreign exchange value of the US dollar against a subset of the broad index currencies that circulate widely outside the US.

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