RESOLUTE FINANCIAL

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Resolute Connections

Since last week's market correction was caused primarily by the continuing spread of the Coronavirus (COVID-19) worldwide, and this week may be equally volatile, we wanted to get this month's newsletter out early and provide some information on the virus and the markets. The three articles below summarize what we know about COVID-19 so far, sheds some light on the current market correction, and puts the talking head's predictions currently occupying the airwaves in perspective.

If you have any questions about anything we have covered in the articles, or a specific situation please feel free to give us a call, or visit our website, www.ResoluteFinancial.com.

The Pandemic: What We Know So Far

The COVID-19 virus has been reported in the national press as either a political or an economic story. It has been compared to the 1917-18 Spanish Flu that infected an estimated one-third of the human population and killed an estimated 50 million people, even though we are now in a very different medical world, even though the Spanish Flu occurred during a major, brutal world war.

As citizens, investors and (so far) healthy individuals, what do we need to know about this new pandemic?

COVID-19 (formally SARS-CoV-2) is a respiratory virus, caused by a new type of coronavirus (in the same family as the virus that causes the common cold) that was first detected in Wuhan City, Hubei Province, China, and has now been detected in 57 locations nationally, including fewer than 100 in the United States. One of its primary features is how contagious it is; the virus can live for hours in a dormant state on surfaces (like a doorknob) after an infected person touches them. It is spread through the air in microscopic droplets when people breath, cough or sneeze. The Center for Disease Control recommends that people who have the virus wear a mask to protect others, but have said that wearing a normal facial mask doesn't prevent people from getting the disease.

In most cases, the symptoms of the disease appear within five days, but there have been reported cases of a 14-day incubation period. Because people can be contagious for up to two weeks before they show symptoms, the virus is very hard to quarantine. This became more evident when it was discovered that a dog had been infected, meaning that it's possible for animals to transmit the disease back and forth with humans. The International Journal of Infectious Diseases, studying the COVID-19 cases from the Diamond Princess cruise ship that reported 355 passengers who contracted the virus, calculated that each person who is infected with the disease, on average, will infect 2.28 others.

As of Friday, there were 83,774 reported cases worldwide, and 2,867 fatalities. The World Health Organization officials have recently increased the risk assessment to the highest ("very high") level of risk assessment in terms of spread and impact.

Reported illnesses have ranged from mild to severe. Researchers from China's Center for Disease Control have recently released the clinical findings of more than 72,000 cases reported in mainland China. The overall death rate is 2.3%, but different populations are far more likely to suffer fatalities than others. An alarming 14.8% of patients 80 and older died from the disease, and 8.0% of patients aged 70-79. At the other end, 81% of the cases in the study were classified as mild, meaning they did not result in pneumonia or resulted in only mild pneumonia.

Fatality rates for children 0-9 years old so far is zero, and the rates are not high for people in younger age ranges: 10-39 years old (0.2%), 40-49 (0.4%), 50-59 (1.3%) and 60-69 (3.6%).

There may be a vaccine on the way, though it is uncertain how soon. China's Clover Biopharmaceuticals is partnering with GlaxoSmithKline on a protein-based coronavirus vaccine candidate called COVID-19 S-Trimer. The University of Queensland in Australia announced a vaccine candidate, and globally, at least 10 other vaccine initiatives are under way. Treatments for people who have already contracted the disease are as yet unproven. An antiviral drug called Remdesivir, manufactured by Gilead Sciences, is being tested on 700 sick patients in Wuhan. A drug called Kaletra, produced by AbbVie to treat HIV, is also being tested.

From an economic standpoint, any industry where people gather together in large numbers is being impacted. That means airlines and the travel/tourism industry generally, plus conferences.

The other impact is related to supply chains. China's quarantine efforts have reduced manufacturing in the country where many global companies have outsourced their manufacturing and assembly activities. Hong Kong is already in a recession, and The Boeing Center at Washington University in St. Louis has estimated a $300 billion impact on the world's supply chain that could last up to two years. Lower demand from Chinese buyers has caused a decline in oil prices.

Prevention efforts and quarantine efforts are certain contribute to the economic slowdown. Japan's Prime Minister Shinzo Abe has ordered all schools closed in Japan for the next month, and officials there are concerned about the possibility that the 2020 Summer Olympics could be curtailed or cancelled. South Korea has shut down numerous educational institutes including elementary schools in Seoul. In Italy, the Lombardy and Veneto regions (total population: 50,000) have been locked down in quarantine procedure following an outbreak in the town of Codogno. U.S. technology companies have expressed worries about disruption to their production in facilities in China, and a February 27 Goldman Sachs forecast suggested that American companies will experience zero earnings growth (Note: this does NOT mean zero earnings) in 2020.

The most important thing to know about the new pandemic is that we actually don't know what the impact will be—on our health, on our nation's economic health, on our portfolios. We do know that the U.S. securities markets are down 11-12% from their recent highs, based on what can only be described as panic selling by the traders who make up most of the volume on the exchanges. That means stocks are cheaper to buy now than they have been, and dividends are higher, as a percentage of share price, but whether that panic will continue, or not, we simply cannot say.

Please understand that we are monitoring the situation, with an understanding that, historically, trying to time the market or make bets based on guesses about the future has been a losing strategy.

Perspective on the Panic

Back in 1987, right after the markets had experienced the famous "Black Monday" decline which took the Dow Jones Industrial Average down by 22.6%, the weekly Barron's financial publication featured, on its cover, a suitcase with the frightened eyes of a Wall Street broker peeking out of its dark recesses, and an arm reaching out to wave a white flag.

After the worst market week since the 2008 financial crisis, and one of the worst months since the 1930s, that image represents how a lot of professional brokers and traders are feeling right now. The market finished out a remarkably bad week of negative returns, including consecutive days of 1,000 point drops in the Dow and a February 1-month drop of 7.5% in the S&P 500 index.

But we hope that is not how you're feeling at the moment. Financial planners and advisors are paid to take on the worst fears of their clients, and it is a burden when unanticipated black swan events rattle the traders who bid stock prices up or down.

If you're open to hearing the good news, then consider that the actual value of the companies that make up the major indices are almost certainly not 10% less valuable today, as businesses, than they were last Monday. The market drop is a panic attack, pure and simple, and real valuations should eventually reassert themselves. The bad news is that neither we nor anyone else has any idea how long the panic attack is going to last, or exactly what those real values are, and we don't yet know whether the triggering event—the Coronavirus, more precisely COVID-19—will spread into a pandemic, and if it does, how much damage it will do to the world economy.

Remember, to date fewer than 200 people have been diagnosed with the virus in the United States. Doesn't it seem a bit early for a panic attack?

Our wish is that you and your family will stay well, and that the virus will not become the pandemic that many (including market traders) are fearing. And please understand that we (and everyone else) don't know what the market will do on Tuesday or next week. The panic might continue, or we might experience a quick recovery. Historically, the best plan when bear markets present themselves is to sit tight, and our goal for you is to follow the best plan we know and wait for the recovery.

Rating "Sure Things" and Holding Soothsayers and Economists Accountable

As the markets go through an entirely normal correction process (triggered, we believe, on a definitely not-normal viral epidemic), it is interesting to go back and look at the people who say they predicted this downturn. One of the jokes on Twitter among professional investors these days goes something like this:

Bears then:

Dow 23,000 - "This is the top!"
Dow 24,000 - "This is the top!"
Dow 25,000 - "This is the top!"
Dow 26,000 - "This is the top!"
Dow 27,000 - "This is the top!"
Dow 28,000 - "This is the top!"
Dow 29,000 - "This is the top!"

Bears Now:

Dow 25,000 - “Told you!”

More broadly, an economist named Larry Swedroe compiles an annual list of predictions that market gurus make at the start of the year, teases out the “sure thing” predictions that were made, and then looks at the end of the year to determine their accuracy.

Among the January 2019 predictions: U.S. economic growth will continue strong through the year, slowing slightly from 3% to 2.7%. Actually, the full year growth rate ended up at 2.3%. This sure thing was wrong.

Corporate profit growth would continue to be strong; S&P 500 earnings would reach $178 a share, up about 8%. Actually, operating earnings fell to $162. Wrong again.

Bloomberg gathered 14 forecasts whose prediction was that the S&P 500 would go up 11% for the year. The 11% forecast was off by about 20%, but Swedroe generously gave this one a “right” score.

Longer-term bonds were predicted to outperform. They did; long Treasuries returned 14%, compared with intermediates at 6%. This one was pretty much on the money.

Fed policy and the European Central Bank unwinding its easy monetary policy would cause the dollar to weaken vs. the euro. The dollar finished the year slightly stronger. Wrong prediction.

Concerns over massive budget deficits and a weaker outlook for the dollar would lead to a strong performance for gold. Gold did go up about 15%. This one was more or less on the money.

Due to the Brexit challenges and various U.S.-initiated trade wars, the VIX index and volatility generally would spike. As it turns out, the VIX finished the year well below its 2018 ending value. Wrong.

Final score: four winners (and Swedroe was generous) and four losers. There's a chart that shows each year's "sure things" going back to 2010, showing that the sure thing predictions were right just 34% of the time. Remember this the next time somebody tells you they "knew" the market was going to fall, or that they know what's going to happen next.

Source:
Bob Veres Inside Edition Newsletter

For more information on these topics or for a free consultation, contact Resolute Financial, LLC at (978) 463-8771 ext. 1003.

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