Raymond Capital Advisors LLC

April 19, 2020

Market Review: A Black Swan Emerges

Stock & Bond Benchmark Annualized % Total Returns
For Periods Ending March 31, 2020

	QTR	1-Year	3-Years	5-Years	8-Years
S&P 500	-19.60	-6.98	5.10	6.73	10.15
Bloomberg Barclays U.S. Aggregate Bond	3.14	8.94	4.83	3.37	3.27
60/40 TAA Composite Index	-10.88	-0.39	5.32	5.63	7.57
3-month Treasury Bills	0.26	1.67	1.65	1.09	0.70

Sources: S&P Dow Jones Indices, Morningstar, Federal Reserve.

The coronavirus (COVID-19) pandemic that emerged in Q1:2020 sent global stock and credit-sensitive bond markets into sharp declines as economies were put into self-induced recessions to prevent health care systems from buckling. In the U.S., the shut-down led to one of the fastest stock market declines on record, going from record highs to a decline of -34% in just 23 trading days. It was a true “black swan” event, both highly unpredictable and extreme in its consequence.

But the abrupt shock to the U.S. economy and financial markets was also enough to elicit massive injections of liquidity and stimulus from the Federal Reserve and fiscal authorities to keep the economy and financial markets liquid, and businesses and consumers in place until it’s safe to return to work. In total, the combined monetary and fiscal stimulus for the U.S. to combat the effects of the coronavirus is estimated to be a whopping 30% of GDP, with even more under discussion. By comparison, the sums dedicated to the initial relief and stimulus for the Great Financial Crisis of 2008 was only about one-fifth the size (6.5% of GDP). Today’s stimulus is massively larger and is also being implemented faster thanks to what was learned from the 2008 crisis! Major European countries are also dedicating about 17% of GDP to their relief and stimulus efforts.

During the market’s rout RCA maneuvered its fixed income strategy towards higher credit quality and shorter duration securities until the Fed had substantially enhanced credit market functioning. Within the equity strategy, steps were taken to temporarily mitigate volatility relative to the benchmark, with the strategy being fully restored once the market began to produce positive returns. The equity portfolio is currently over-weighted in Medical, and Utilities; and under-weighted in Finance, and Retail/Wholesale sectors. For tactical asset allocation, a modestly higher amount of equity exposure (above benchmark neutral 60%) was adopted in the week following the March 23rd stock market lows; and, as the market continued to rebound, we have permitted the RCA Tactical Asset Allocation strategy’s equity exposure to drift up to 66% of total strategy assets, while underweighting bonds at 34%.

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Outlook: The Healing Process

Our views have not changed much since our interim client letter of March 22 (one day before the stock market bottomed). The good news is that the worst of the stock market decline is now likely behind us as our indicators have registered deeply oversold readings, climactic selling, and favorable upside thrusts conditions. This does not rule out future pullbacks in stock prices. But with near zero percent interest rates, enhanced credit facilities for market liquidity, and "unlimited asset purchases" announced by the Fed, as well as unprecedented amounts of fiscal stimulus, it's a reasonably high probability the market's lows were seen in late March. Moreover, computer trading algorithms have likely helped to speed-up the market's recovery. Indeed, just as we witnessed record velocity into a bear market during the February-March slide, we also experienced a return to bull market territory in record time with stocks now up more than 28% in just 18 trading days!

Beyond the market's recent rebound, however, we caution that economic fundamentals are at risk of deteriorating the longer the economy stays in lock-down. Growing public sentiment against buybacks, a key bullish driver of stock returns, and the upcoming presidential election also adds policy uncertainty. There are also increased risks from "unknown unknowns" as crisis environments can be breeding grounds for black swan hatchlings (witness the recent oil price collapse). So, unless we can: 1) significantly scale up testing and sort out the at-risk versus immune populations, 2) add rapid response contact tracing, 3) and/or develop effective therapeutics and vaccines to prevent a second wave of infections, or 4) keep the economy sufficiently backstopped, the economy's healing process may become elongated, and the upside for stock prices also limited.

Thank you for your continuing support.

With best regards,

Geoff & Lance

Raymond Capital Advisors, LLC
A Retirement Wealth Advisor