Argent
Wealth Management, LLC

Investment Outlook
Spring 2020

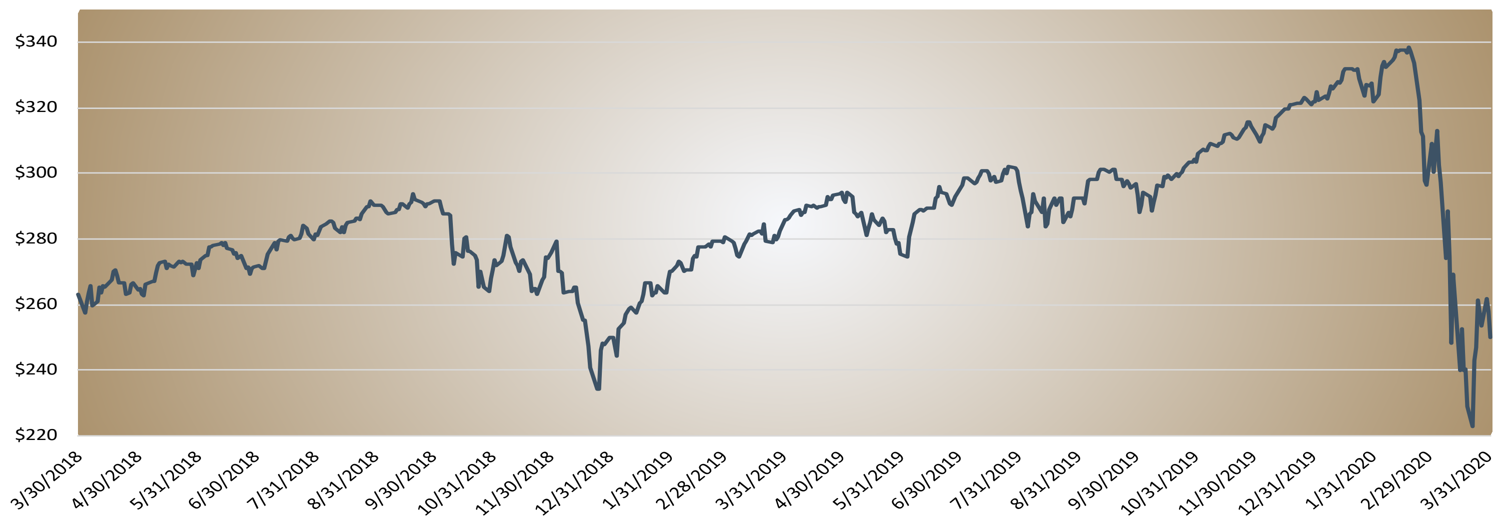
First Quarter 2020 Review; Second Quarter 2020 Outlook

A Quarter of Unprecedented Events: Now What?

What Happened

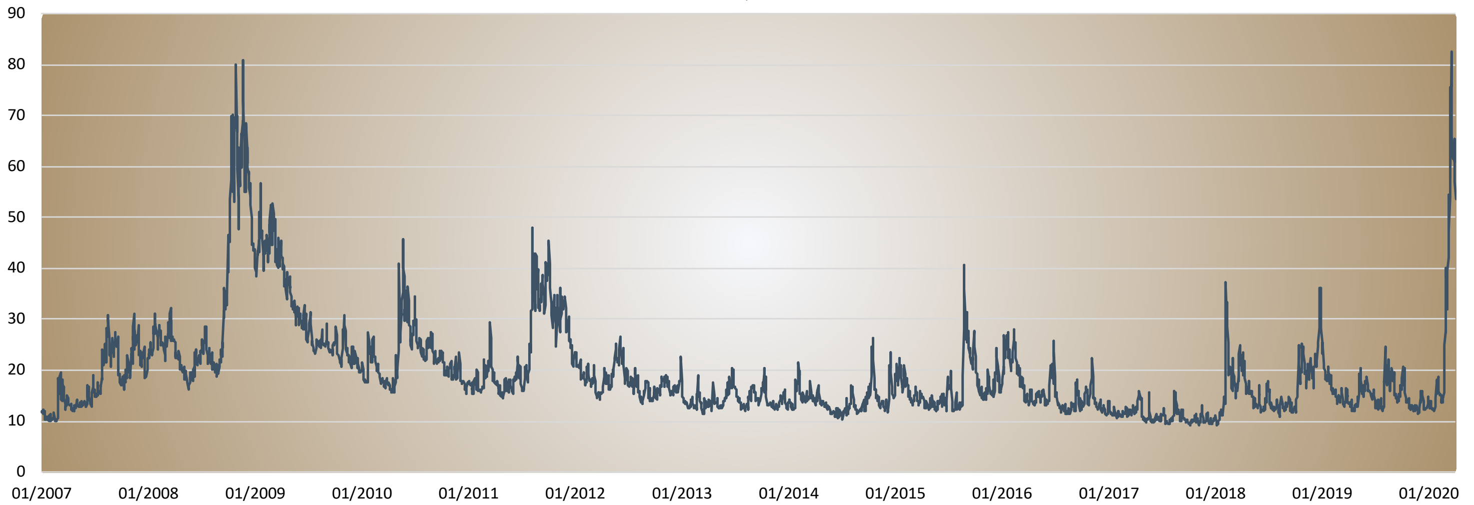
In our first quarter 2020 version of this newsletter, we recommended investors enter 2020 with caution. This has proved to be sound advice. Our recommendation was based primarily on indicators that implied investors were overly optimistic and valuations were high. Little was known about a virus that was first reported on January 10 and was starting to spread in China. When the novel Coronavirus (COVID-19) began to spread, China enacted draconian measures to contain it and quickly built hospitals to treat infected patients. These measures were an indication of things to come. The U.S. now has more cases than China; per Worldometers.info, China has ~82,000 cases and the U.S. has ~ 190,000 cases as we write this on April 1. The U.S. federal government did not act with the same aggressiveness as China when cases started to spread in the U.S. However, it quickly became apparent that without physical distancing the virus would spread so rapidly that the healthcare system would be overwhelmed with patients. For this reason, the federal government and the states started to recommend and implement—and in some instances require--physical distancing measures which continue to evolve. It quickly became apparent that physical distancing would have an astonishing and negative impact on the economy.

SPDR S&P 500 ETF (SPY)



Source: Factset: Argent Wealth Management, LLC © 2020

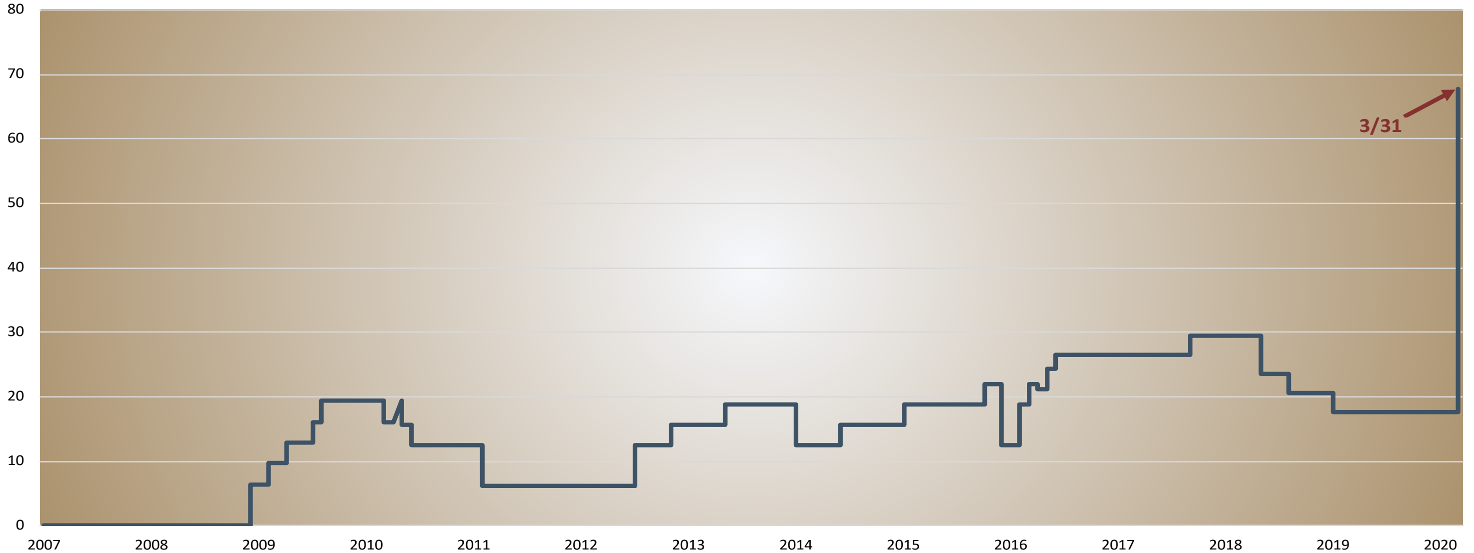
On February 9 the S&P 500 was at 3370, and on March 23 it was at 2230, a 34% decline in 43 days. This was the swiftest decline of over 30% since World War II. A recession has no doubt started. On the week ending March 21, 3.23 million people filed for unemployment benefits, about 5x the record previously set in 1982. It is not surprising that the VIX, a measure of fear, implied investors became more worried than they were at the height of the 2008 Global Financial Crisis (GFC). The question is how long and how deep will the recession and stock market correction be.



Source: Factset: Argent Wealth Management, LLC © 2020

Global Government Response

The Federal Reserve (The Fed) acted quickly to lower the Federal Funds rate to .25% and enacted unlimited quantitative easing, vowing to do whatever it takes to keep funding markets liquid and the financial system operating smoothly. The Fed's balance sheet, one way to measure how accommodative they are, grew by over $1trillion or about 25% in the past four weeks (according to federalreserve.org) to over $5 trillion for the first time in history. Fed Chairman Jerome Powell went on the Today show on March 26 to tell the world that they have plenty more they can do. Globally, 70% of central banks around the world are at record low target interest rates, a record according to Ned Davis Research.



Source: Ned Davis Research, Inc.

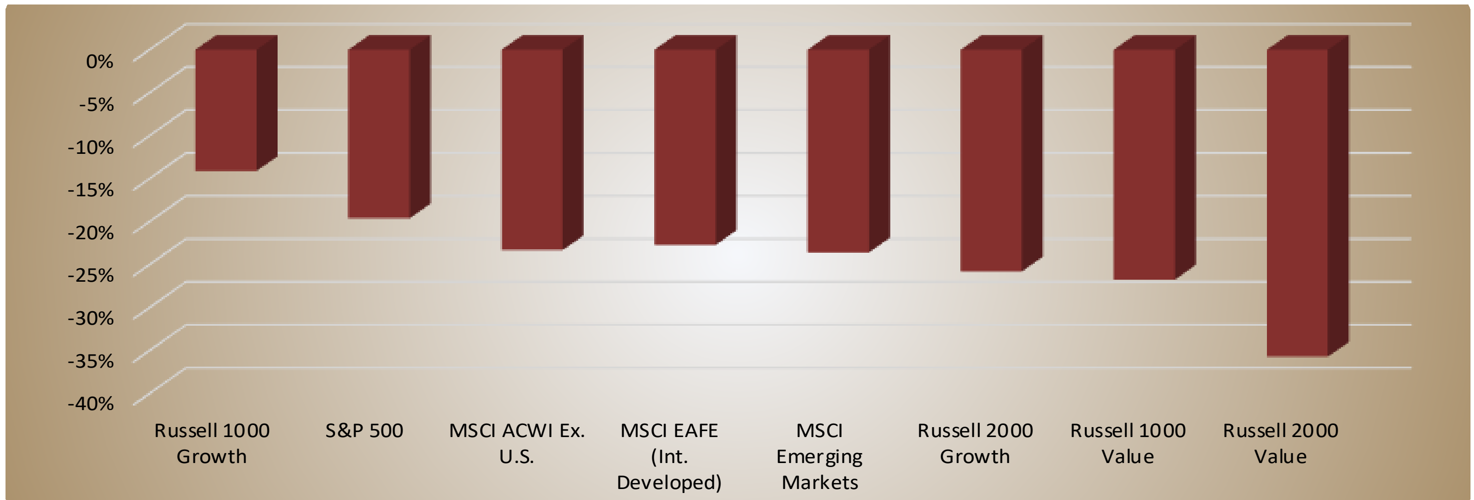
The federal government enacted a $2 trillion fiscal stimulus package, which represents about 10% of Gross Domestic Product (GDP). The stimulus includes increases in unemployment insurance, direct checks to households, and direct loans to businesses, some in the form of grants for those that retain their employees. For comparative purposes, during the 2008-2009 GFC, fiscal support maxed at about 6% of GDP. The type of stimulus enacted, broadly speaking, differs from 2008's programs in that more is going directly to consumers and businesses immediately. This makes sense given the immediate and stunning impact the pandemic has had on the world economy. But other countries have yet to enact fiscal stimuli as they did in 2008. Notably, China, which enacted a fiscal measure in 2008 that amounted to 11% of GDP, has done nothing widespread yet. The S&P 500 went up 17% over three days from March 23-26 in response to what the government and central banks had done so far.

Algorithmic trading may also be contributing to the precipitous up and down movements of the market. According to the Tabb Group and the Financial Times, approximately 60% of trading is a mix of high frequency traders and quant strategies. Many of these strategies look at similar market technical triggers when trading. When these triggers are hit, they sell en masse. This can exacerbate market movements both up and down, especially in times of uncertainty. Thus, dislocations between the intrinsic value of the stock market and the quoted value of the stock market can occur. This has created, and will continue to create, opportunities for disciplined objective fundamental investors like Argent.

Stock and Fixed Income Returns

The Russell 1000 Growth index, down 14%, outperformed all other major indices in the first quarter. Technology, which accounts for 34% of that index, was down 12% making it the best performing sector. Remote work isolates technology from the pandemic's impact relative to other sectors. Large Technology stocks only account for 7.4% of the Russell 1000 Value index, and 10.5% of the MSCI All World (ACWI) Ex U.S. index.

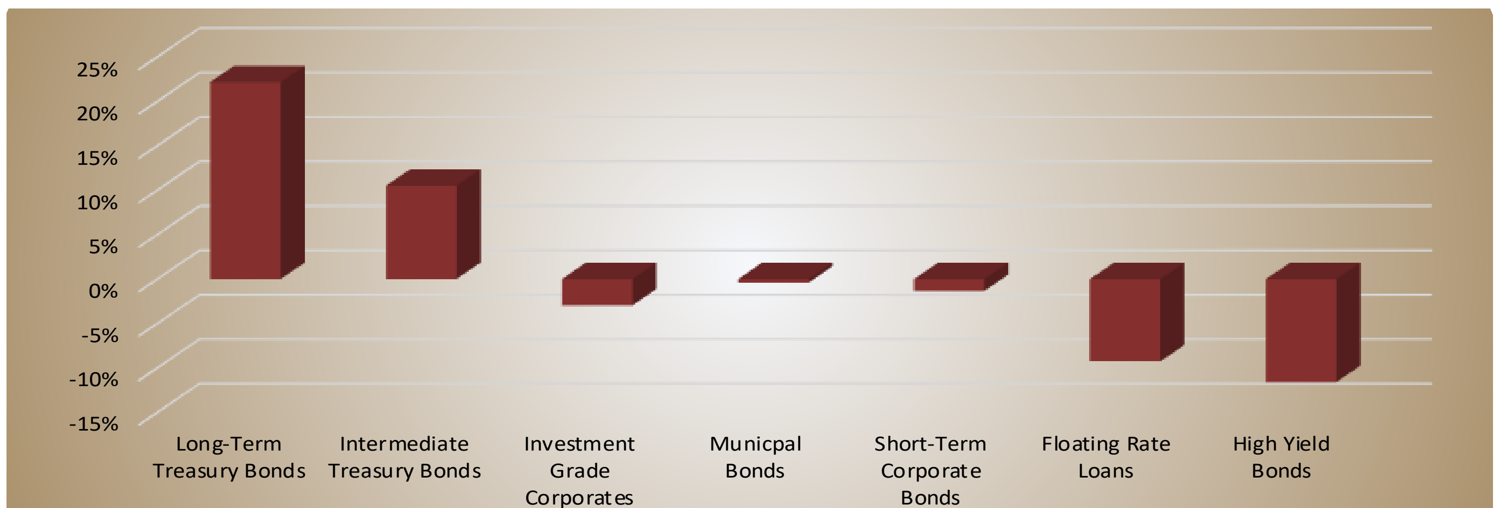
Equity Returns YTD



Source: JP Morgan

U.S. Treasury bonds dated ten years and beyond outperformed as investors preferred their perceived safety over corporate bonds. Non-investment grade corporate bonds, or "high yield" bonds rated BB or below, and non-investment grade floating rate loans were the worst performing fixed income sectors. Exposure to rising default rates and their lack of liquidity compared to investment grade bonds sent them both down sharply on the quarter.

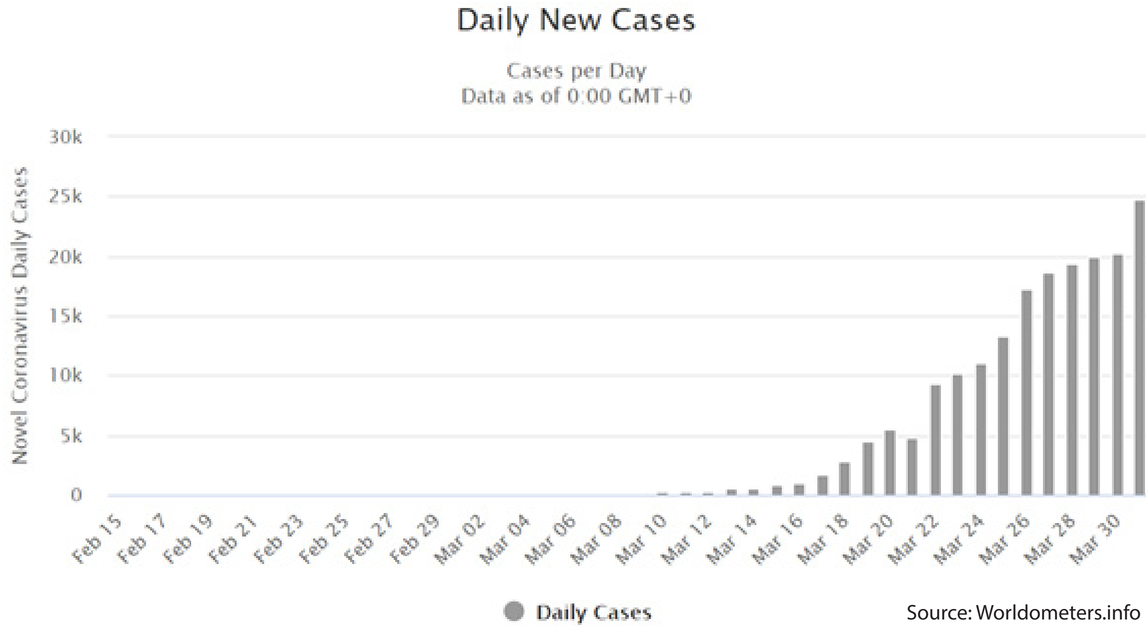
Fixed Income Returns YTD



Source: FactSet, based on representative ETFs

What is Next, and What to Do

This is the first time a pandemic has caused a major halt in the world economy, so uncertainty abounds. Investors tend to sell when uncertainty increases. When the pandemic first showed signs of spreading through the U.S., uncertainty was at its highest, and this coincided with VIX, a measure of investor fear, skyrocketing to record levels. Uncertainty has decreased as governments enacted stimuli and gave direction on how they will attempt to deal with the spread of COVID-19. Unfortunately, the question we still can't answer definitively is how much more the virus will spread.



Currently, it appears cases are increasing at an accelerating rate. Until investors and health experts see cases rising at a decreasing rate consistently, forecasts will continue to have wide error bands. Over time, as testing becomes more available, data will become more reliable and we can understand the path of the virus better. That data will be crucial for government, individual and business decision-making. Uncertainty and volatility will decline only when markets can more accurately price in the economic impact of the pandemic and governments can accurately calibrate their monetary and fiscal response. Of course, the best news would be an FDA-approved, effective treatment and progress on a vaccine.

While we wait for more data, markets are likely to remain volatile. Investors that are well positioned within their long-term investment plan should look at corrections and volatility as opportunities to rebalance portfolios and take advantage of dislocations created by uncertainty. This is precisely what we are doing at Argent. This pandemic will pass. Markets are a leading indicator, so they will start to recover before COVID-19 abates. History has taught us that stocks and economies are resilient and both will bounce back. Every major correction is caused by a different shock, but since WWII, after a quarter where the S&P 500 is more than 15% down, in 100% of instances six months, one year, and two years later the S&P 500 is up compared to the close at quarter end with a median return of 23.5% over one year and 43% over two years.

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All of us at Argent thank you for your continued support and confidence. If you know of anyone that might benefit from Argent's services, we would welcome the opportunity to discuss their particular situation with them.

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