March 20, 2020

Dear client,

I am sure that the last couple of weeks have been nerve-wracking for you in regard to your investments and most likely the disruption to your lives. That's why I wanted to get this letter out to you before the weekend. I want to let you know that I have been in constant contact with my trusted strategists at BCA Research and Alpine Macro. By carefully reading their research reports and talking to them, it helps me keep a level head. In times of financial stress, it is very beneficial to have trusted individuals with whom you can bounce ideas off. Lucky for me, I have those resources at BCA and Alpine. In one way or another, BCA, Alpine and myself have had a relationship since 1998.

I have been busily working at home during the day and into the night analyzing the market financial conditions and that of our stocks. In this process, I have dusted off my collection of financial history books and have also consulted my old graduate school notes to see if there are any similarities between the 1918 influenza, other market crises, and the response.

As far as history goes, it looks like the stock market fully recovered from any major financial crisis within 15 months. In today's case, it may be much shorter. There are three types of recessions: a balance sheet recession, a Fed engineered recession and a supply/demand shock recession.

- **Balance Sheet recession**- When the banking system gets impaired. For example, in 2008 when real estate crashed and pulled down everything.
- **Fed engineered recession** - This is when the economy gets overheated, stock market gets overvalued, and the Fed raises interest rates to slow the economy down.
- **Shock recession**- A good example of this is the 1973-1974 oil embargo and now the coronavirus pandemic.

In a shock recession like this one, the recession may be shorter and therefore the stock market recovery should be shorter. I suspect by the end of the year, because of all the liquidity in the system, the market will recover faster.

No one really knows how long this COVID-19 pandemic will last, but there are certain facts that I do know. First, the stock market will not go to zero, but it is possible that it could go down another 10% to 15% from these levels. Second, after all this stimulus is finished, I suspect inflation will start to rise and the Fed will let it run loose.

The big question is, what am I going to do? As Senator Elizabeth Warren says, "I have a plan." In my opinion, we are in good shape because we were cautious about the over extended stock market before the coronavirus hit. In my segments of "Coffee with Dr. Steve", I have said for a few months that the U.S. stock market was overvalued, overextended, and overbought. This cautiousness led me to reduce the stocks in the portfolio before the COVID-19 virus sprung to life. In retrospect, that move was helpful. Since then, I have trimmed a few stocks as well. When panic occurs, there is a rush to sell everything indiscriminately. This includes stocks, bonds and gold. Some of this is because of fear and some of it is because many speculators who borrowed money to buy stocks had their loans called in. Those speculators have to liquidate their holdings to pay back their loans.

Gold declined due to the loan recalls and the strengthening U.S. dollar. The U.S. Dollar strengthened 8% in the past two weeks and 1.58% on Thursday alone. This is a new record. However, after the government voted on their stimulus package, the dollar started to decline, and gold should recover.

We are cautious, deliberate and thoughtful, but we are **not** in panic mode. We may be near a bottom, but I don't know that with any certainty. I have plenty of firepower in cash and bonds and I will increase the allocation of stocks when the time is right. Many are trading at ridiculously low prices right now. I have 109 individual stocks on my radar screen as we speak. When it is appropriate, I will increase our stock exposure and I don't plan on selling much from this level unless I absolutely have to, in a worst-case scenario. This is not my base case scenario.

Most likely, when then pandemic is over and the economy has fully recovered, we will have to tilt the portfolio towards more inflation resistant stocks, increase our gold and concentrate on inflation protected bonds.

Due to working from home, we are not able to do our weekly Coffee with Dr. Steve. However, for everyday market updates, please follow me on Twitter: @StevenYamshon.

Most of us are now working from home and you can call our regular telephone number 949-251-9333 and it should ring at one of our houses. Just in case, my cell phone is 310-270-5256.

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We invite you to tune into our next conference call on **Tuesday, March 24, 2020 at 6:30 p.m**. To join the conference call, **please dial the toll-free number: 1-800-914-8405. Once prompted, enter the access code: 5486434, followed by the # button**.

Steve Yamshon
Managing Principal

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