Weekly Capital Market Comments

March 2, 2020

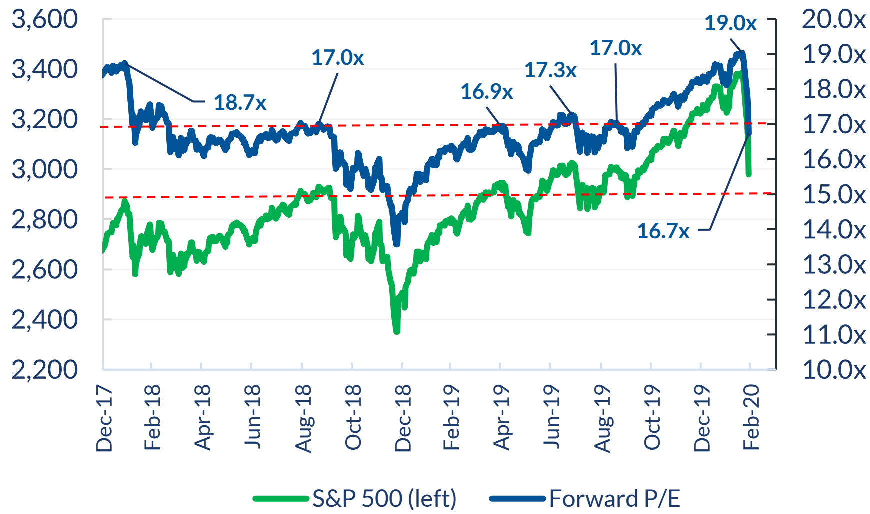
NORTHEAST SEQUOIA
PRIVATE CLIENT GROUP

Fashionably Late Or Dimwittedly Early?

Equity markets fell ferociously this week (Thursday through Thursday). Over the last five trading days, the S&P lost 11.7% and now stands down almost 8% YTD. The forward P/E multiple for the S&P has fallen over two turns, to 16.7x from 19.0x only two weeks ago. Global markets have not fared much better, with most of Europe off over 11%, while interestingly, several Asia-Pacific equity markets saw more moderate sell-offs. The Energy sector here in the U.S. was off 18% over the last week, while Technology and Financials were down by 14% and 12%, respectively. Even Staples were down by over 8%. The sector/style that did the best this week was Preferred Equities; the iShares Preferred ETF was down only 3.7%. The 10Y U.S. Treasury finished Thursday's session at 1.27%, down from roughly 1.92% at the beginning of the year.

As we pointed out in our January 31, 2020, weekly note, "The Punch You Don't See Coming," unmeasurable consequences associated with the Coronavirus epidemic may result in a deeper sell-off given the fact that previous outbreaks occurred during the middle of an economic expansion or closer to a trough, and not at the height of market valuations. Further, in last week's note, "Cut To The Chase," we highlighted the fact that equity market participants continue to wait with bated breath for relief from central banks. At that time, we observed one, maybe two cuts by the end of the year. Now we are observing as much as a 75bps (0.75%) reduction in the Fed-Funds rate by year-end. If you ascribe to these expectations, some believe the next question is, does the Fed cut 50bps in March, or only 25bps?

S&P 500 | P/E Now At Our Upper Bound of 17x



Source: FactSet and NEPCG

But we believe the next question is, "When do we start moving back into equities?" We have been telling clients all week that we'd rather be late to a great party, than early to a dud. However, for us to get more bullish, we still need to see more panic in the market. We remember back at the beginning of the 2006-2007 downturn; we first realized fear set into capital markets when money-market funds were priced below $1. We don't see that type of panic yet, despite a spiraling-down in the short-dated interest rates. Further, we believe it may be too pollyannaish to think that all the S&P needs to do is trade down to its long-term average of 15-16x, or that a 50bps rate cut will solve the problem. Perhaps we need to see a 14-handle, accompanied by near-zero growth in earnings, versus the current 4% year-over-year expectations. **We think it is a mistake to assume things can't get worse, but we are starting to believe a bottom may be near.** We'd love to hear your thoughts.

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