Ginsburg Financial Advisors, Inc.
Personal Financial Planning & Investment Management
Larry P. Ginsburg, CFP® **Adele Ostomel, CFP®**

phone: **(510) 339-3933**
fax: (510) 339-1611
LGinsburg@GinsburgAdvisors.com
AOstomel@GinsburgAdvisors.com
www.ginsburgadvisors.com

What are the Implications of the Coronavirus?

Fears over the spread of the coronavirus (officially named COVID-19) from China to the rest of the world has resulted in a global stock market sell-off. The recent downdraft in global stock prices has generally been less impactful to our clients' portfolios due to our decision to tactically reduce risk in 4Q 2019. While the spread of COVID-19 is unfortunate, the economic impact of this situation is expected to be largely transitory. We anticipate global stock prices will begin to recover what was lost when there is increasing evidence for global containment of COVID-19 over the coming weeks.

What is COVID-19?

COVID-19, or coronavirus disease 2019, is an illness caused by the virus called SARS-CoV2. The outbreak of COVID-19 has been traced to an exotic animal market in Wuhan, the capital of Central China's Hubei province. The virus is thought to have "jumped" species from animals to humans and is thought to be transmitted between humans via physical contact with air drops (e.g. inhaling air droplets expelled from an infected patient's sneeze, cough, or breath exhalation). There is no evidence to date that SARS-CoV2 is transmitted through the air. The virus causes a pneumonia-like illness deep within the lungs but does not present with upper respiratory symptoms like the runny nose typically accompanying the flu or common cold.

As of February 27, there were 83,113 confirmed cases of COVID-19 globally with 95% of these cases occurring in mainland China (worldometer). The fatality rate for this disease is currently 3.4%, but this value is skewed higher by the fatality rate within China of 3.5% (worldometer). The fatality rate outside of China is 1.6% (worldometer), which is much lower than the fatality rates for the 2015-2016 Zika pandemic (8.3%), the 2012-2013 Middle East Respiratory Syndrome ("MERS") epidemic (35%), and the 2002-2003 SARS epidemic (10%). Most of the deaths caused by COVID-19 have been in elderly patients previously in poor health. Encouragingly, 37% of infected people in mainland China have recovered without clinical intervention, and this number has been trending higher by 2% to 3% each week (Neuberger Berman). The data referenced does not include an expected amount of people who had mild symptoms and as a result did not report being sick. This knowledge probably results in a much lower mortality rate than has been reported.

Confirmed Cases Are Slowing in China so Why Are Investors Still Nervous?

Incremental confirmed cases of COVID-19 within China have slowed over the past seven days. This suggests China's overwhelming response to containing the disease, which included forced quarantines and the shutdown of travel between numerous cities and provinces within Central China, has been effective. The financial markets, however, will not be comfortable until

6201 Medau Place, Suite 101, Oakland, CA 94611

there is concrete evidence regarding the durability of this trend especially as more and more mainland Chinese residents return to work and school.

Investors are also concerned about the recent jump in confirmed cases in South Korea, Italy, and Iran. Specifically, there are clusters of disease within these countries that have no clear epidemiological connection to China suggesting COVID-19 has flipped the switch to community transmission. This means the virus may be spreading untraced throughout the world and is most likely already in many places, but we just do not know for certain where COVID-19 has migrated. This is what prompted Dr. Nancy Messonnier, a director at the United States Centers for Disease Control and Prevention ("CDC"), to declare: "It's not so much a question of if this will happen anymore, but rather more a question of exactly when this will happen" in the US.

The connection between the spread of COVID-19 and the financial markets has to do with the perceived impact the disease will have on global economic growth, which was just starting to recover from a worldwide contraction in manufacturing (spurred on by the recent US-China phase 1 trade deal). Investors are also concerned about the impact this disease will have on corporate earnings, especially for companies that derive a meaningful share of revenue from China while also experiencing material disruptions to their global supply chains.

Market fears over the spread of COVID-19 has resulted in a "correction" in excess of 12.0% (as of the market closing prices on February 27, 2020) to US stock prices, as measured by the S&P 500 Index, since reaching their high on February 19, 2020. Outside of the US, foreign stock valuations, represented by the MSCI ACWI ex US Index, experienced a 9.4% "pull back" since reaching their respective high on January 17, 2020.

The contraction in global stock prices has driven bond yields lower as investors implement a "flight to safety" away from stocks. The Bloomberg Barclays US Aggregate Bond Index has risen 4.1% year-to-date through February 27, 2020, due to higher demand from investors seeking to "de-risk" their portfolios by owning more investment grade bonds. We generally increased client exposure to these types of bonds in the 4th quarter of 2019 to protect principal.

Preventive Portfolio "Medicine" (Risk Reduction) Continues to Help

Generally, we took advantage of strength in the financial markets near the end of last year to tactically reduce risk in many of our client portfolios. We deemed this reduction in stocks to be prudent considering heightened stock market valuations did not adequately discount the potential for a lingering slump in global manufacturing activity. Further deterioration in global manufacturing trends was possible if China did not follow through with the purchase commitments it made as part of the US-China phase 1 trade deal. We were also concerned over the potential for heightened stock market volatility going into what is to be a very contentious presidential election cycle.

As we discussed in our fourth quarter 2019 newsletter, we typically reduced client portfolio risk by broadly trimming stock exposure in favor of owning more high quality bonds. We also started to shift the composition of US stock exposure towards high quality, value-oriented stocks that tend to have lower volatility relative to the overall markets, especially compared to “growth stocks.” It is also important to note that for most of our clients, we have reduced US stock exposure over the past two years to a current level that is roughly 50% of what we would normally advocate owning earlier in a rising market cycle. We have also chosen to tactically emphasis stock sectors that tend to outperform the broader markets during the late phase of a business cycle and into a cyclical downturn (e.g. consumer staples and health care).

It is natural for the stock market to experience corrections, especially following the longest bull market in history. We had prepared for this by generally reducing client exposure to US equities, especially growth stocks, during the past year. While we custom tailor each of our client portfolios based on their goals and tolerance for risk, our perspective is that large company US stocks have delivered returns for the last decade that are more than 35% per year above long-term averages.

We recommend ownership in foreign/international large company stocks for most of our clients due to their “reversion to the mean” potential (the average return for these stocks over the past decade is close to 50% below long-term averages). The PIIGS issue (Portugal, Italy, Ireland, Greece & Spain financial problems), Brexit, and other factors have blunted stock prices in Europe in the past decade. This is likely to change in the coming years.

For most clients, we recommend maintaining current holdings in the Emerging Markets (“EM”) (less than 30 of 130 economies that have an average annual per capita income below $25,000). The EM sector has delivered average returns during the past ten years of less than 40% per year compared to long-term averages. As the global recession ends, we expect the EM sector to be one of the leaders. There are now consumers in the EM countries so some of what they produce is consumed in the countries making these products; formerly production was all sent overseas into the developed markets.

Presidential election years are normally good for stocks. Once the election results are known, the financial markets appreciate the “certainty” of knowing the policies that may be implemented in the near future. In 2020, we expect more volatility than in a normal presidential election year, given the variety of candidates and the lack of coherent policy emanating from Washington D.C. This has caused us to be more cautious than normal during a presidential election year.

This Too, Shall Pass

It is important to note that the US and China account for approximately 34% of global gross domestic product (“GDP”) (International Monetary Fund). Consumer spending, which accounts for 68% and 39% of US and Chinese GDP (World Bank), respectively, is the driving force behind global economic growth. We acknowledge that the spread of COVID-19 will disrupt global economic growth and business activity during the first half of 2020, but we do not expect consumer spending in the US nor China to be materially impacted for an extended period. Our confidence in the US consumer is supported by robust employment trends and rising incomes while the Chinese consumer is benefiting from the expanding “wealth effect,” especially into lower tier (non-coastal) cities.

As we mentioned above, there have been other medical events, epidemics/pandemics that have caused global concerns. Each time the events themselves as well as the economic impact has been transitory. Given that we have no reason to think that this will not be true with COVID-19, we encourage you to continue to think about the long-term benefits of investing prudently toward the attainment of your goals.

Please do let us know if you have any questions or concerns. We want to make certain that your personal investment portfolio is structured to attain your long-term goals while being able to support any distributions you may need in the near term. Most importantly, we want you to sleep well at night during the process of owning investments that can help you reach your objectives.

What Can You do to Protect Yourself?

We are employing our tactical asset allocation to manage this volatility as best we can for your investment portfolio.

Physically and personally, the best advice medical professionals have given us is repeated handwashing, using soap while singing “Happy Birthday to Me” at least twice. (Use hand lotion if your skin becomes too dry with all the extra washing!)

If you are concerned about social interaction, you might choose not to go to public events (concerts, theater, sports events) you may have planned to attend.

If you are planning to travel abroad, you may want to reconsider going to any place where a cluster of COVID-19 has been identified.

No independent analysis has been performed and the material should not be construed as investment advice. Investment decisions should not be based on this material since the information contained here is a singular update, and prudent investment decisions require the analysis of a much broader collection of facts and context. All information is believed to be from reliable sources; however, we make no representation as to its completeness or accuracy. The opinions expressed are as of the date published and may change without notice. Any forward-looking statements are based on assumptions, may not materialize, and are subject to revision.

All economic and performance information is historical and not indicative of future results. The market indices discussed are not actively managed. Investors cannot directly invest in unmanaged indices. Please consult your financial advisor for more information.

Additional risks are associated with international investing, such as currency fluctuations, political and economic instability, and differences in accounting standards.

Index descriptions:

Standard & Poor's 500 (S&P 500). A market capitalization-weighted index of 500 widely held stocks often used as a proxy for the US stock market. It measures the movement of the largest issues. Standard and Poor's chooses the member companies for the 500 based on market size, liquidity and industry group representation. Included are the stocks of industrial, financial, utility, and transportation companies. Since mid-1989, this composition has been more flexible and the number of issues in each sector has varied.

The Bloomberg Barclays US Aggregate Bond Index, or the Agg, is a broad base, market capitalization-weighted bond market index representing intermediate term investment grade bonds traded in the United States.

The MSCI ACWI is a market capitalization weighted index designed to provide a broad measure of equity-market performance throughout the world. The MSCI ACWI is maintained by Morgan Stanley Capital International (MSCI) and is comprised of stocks from 23 developed countries and 24 emerging markets