

March Madness

My perspectives and thoughts on the chaotic challenges
I anticipate are just around the corner and further down the road

March 19, 2020

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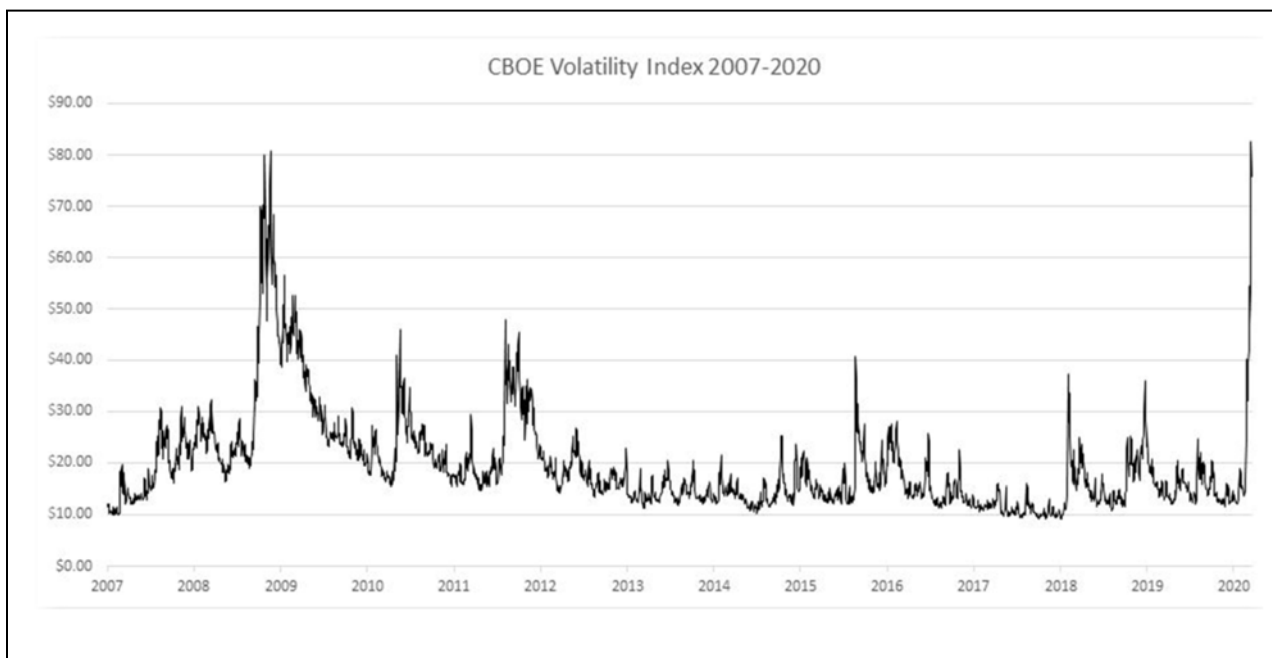
Investment Planning Committee Chair

Winston Churchill is credited with saying, “A pessimist sees the difficulty in every opportunity, an optimist sees the opportunity in every difficulty.” This note will focus on the pessimism I anticipate we will need to manage and overcome in each of our living rooms.

The note that will you will receive next week will focus on optimism and the exponentially growing number of investment opportunities that are being born, almost daily, out of the pain our world is currently experiencing.

At Cal Cap, our best investment outcomes are derived from doing a 360-degree examination of the important issues that impact managing money. We examine the upsides, downsides, short-term ramifications, long term ramifications, intended consequences and potential unintended consequences with equal interest, appreciation and depth on any subject matter that impacts investing. Only then can problems be mitigated – and reasoned investment decisions be made. The following are the chaotic themes and moments to anticipate.

(A) Fear – The Zeitgeist of the Moment



The graph above is referred to as “the VIX,” but in the investment profession we call it the Fear Index.

Fear can make any human operate from the reptilian (survival at any price) part of his brain. Fear can override the limbic (experiences) and neocortex (imagination, language and abstract thought) part of the brain to detrimental consequences. [Side note to the doctors and scientists reading this note: This is not meant to be an exhaustive explanation of the brain.]

We all know that fear can lead to irrational and illogical outcomes. It is the very reason Franklin Delano Roosevelt (FDR) said the following in his iconic inaugural address on March 4, 1933, at the height of the Great Depression:

“This great Nation will endure as it has endured, will revive and will prosper. So, first of all, let me assert *my firm belief that the only thing we have to fear is fear itself* – nameless, unreasoning, unjustified terror which paralyzes needed efforts to convert retreat into advance.”

Fear is palpable in all of our society today. Our best defense and response must come from our emotional competence. If investors can confront and contain their emotions, then reason will allow us to lessen the panic short-term fear creates until the clouds clear.

We recommend implementing a routine of positive distractions. The reptilian brain cannot be allowed to make investment decisions, so give it a break and please repeat often.

To give my mind a break during the Great Recession, I would dedicate a part of each evening to reading. I needed a mental break like anyone else. I also felt the added weight due to the financial futures of hundreds of families, businesses and non-profits depending on Cal Cap’s ability to reason in the face of great uncertainty. That is when I started the habit of reading the entire works of one author before moving on to the next. David Baldacci, Daniel Silva and David McCullough helped me get through those tough times.

Another example: A retired, Type-A client of ours shared his new routine with me earlier this week. Yoga in the morning, meditation in the afternoon and self-administered back therapy in the early evening. He’s also taken to re-watching his extensive movie collection, having been a member of the Academy of Motion Pictures for ages.

Whatever you need to do to confront and put the fear behind you – please do it. Find a routine of positive distractions and keep the reptilian part of our human brain at bay.

(B) Tomorrow 3/20/20 - Quadruple Witching

Please be aware of the possibility of increased volatility tomorrow due to so-called quadruple witching, the Friday near the end of each calendar quarter on which options and futures for both indexes and stocks expire simultaneously. The moves in either direction may likely be exacerbated by the recent market volatility.

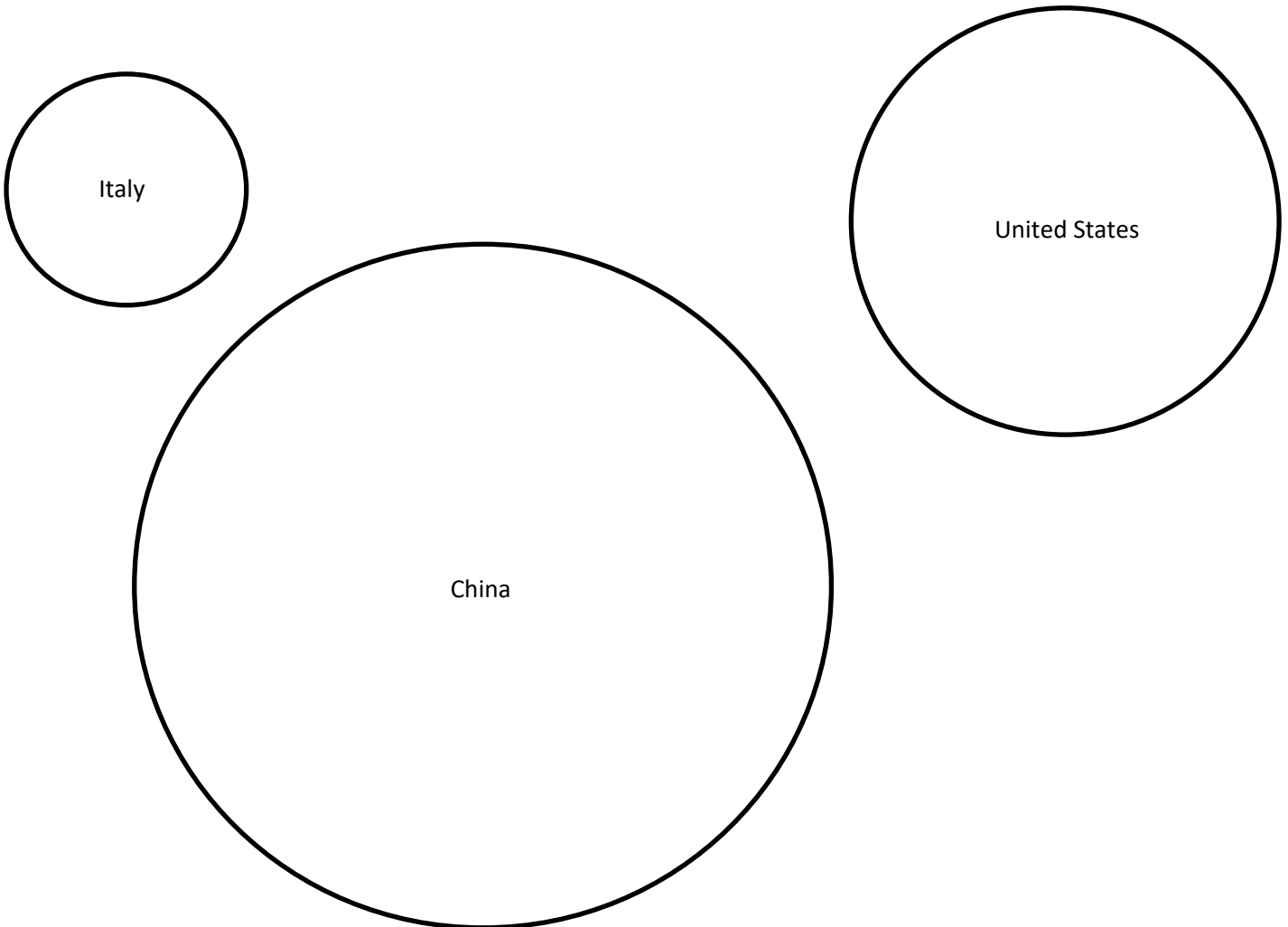
(C) The Coronavirus Numbers are Going to Grow Before They Decline

As testing ramps up and the disease progresses, both new cases and deaths will increase. It will seem far worse due to constant media coverage and lack of context. When Brad and I started at IDS/American Express in the late 1980s, part of our training meant understanding the various forms of risk that investors face. The most well-known being the risk of losing capital. Among the myriad of other types of risk include interest rate risk, regulatory risk, liquidity risk, inflation risk, etc.

The speed of the Internet brought us a new challenge called Headline Risk. This is the risk of information traveling at a high rate of speed and many times in a purposely sensationalized manner. Winston Churchill said it best, "A lie gets halfway around the world before the truth has a chance to put its pants on."

(D) Loss of Perspective

It is easy for anyone to become fixated to the point of becoming emotional, which leads to a warped and inaccurate sense of reality. We all understand the nasty effects of the coronavirus. I simply ask everyone to examine the numbers in perspective. From the smallest to the largest population the circles represent Italy, the United States and China.



In the circles above, I tried to place two dots in each country. The first dot to represent the number of total cases of the virus and the second dot to represent the associated deaths. I say "tried" because my Microsoft Word program and/or printer does not have the ability to make dots tiny enough to be proportionally accurate yet be seen by the human eye.

Take Italy for example, when you divide the number of total cases (about 41,000) by the population (about 60 million) you arrive at 0.000683% of people in that country who have been infected to date. I am unable to provide a visualization of that number in Italy's circle because it's too small. Same for the United States and China.

To be sure, this is a nasty virus that can do us harm. I realize that many people around the globe are losing loved ones. I believe it's going to get worse before it gets better.

(E) Cabin Fever

What will be the consequences of feeling cooped up all day in a free and mobile society? Many times, couples will struggle when just one of them retires and is now home all day. Multiply that across the nation, adding in many people feeling the stress of making ends meet. This allows more time to search out opinions on social media and watch the news, which could end up in hysteria, panic and mania increasing in the coming days and weeks. We know food delivery companies will spike up, and unfortunately, so will domestic violence. This could be a powder keg with a short fuse.

(F) Business Failures

We know that Mom and Pop businesses are going to get hit the hardest, but unless it happens in our neighborhood, we will only hear about the anecdotal evidence. However, when a well-known company begins to lay off people or they cannot pay their bills or debts, that will make headlines.

(G) Temporary Changes to Our Infrastructure

The European Union was the first to call for Netflix and other streaming services to lower the bandwidth they use for fear of "breaking the internet." How will the under-30 crowd deal with the potential reduction of connectivity?

(H) Recency Bias can Ruin the Big Picture

This is the phenomenon of a person only remembering something that has occurred recently as opposed to something that occurred a while back. Take investments for example: Many people will only look at how the volatility has impacted them this month while not giving the same consideration to how much money they have made over the years. Many people will only really think about this latest episode of calamity, not realizing they endured other tough times such as wars, riots, countries collapsing around the world, the dot-com bubble, 9/11 and the Great Recession. And that is to name only a few.

(I) Consequences of the Extraordinary Measures Being Implemented Worldwide

How will these measures impact inflation in various countries? What new regulations will be created to try and prevent this same type of event from occurring in the future? How much new debt will people, businesses and governments add? What new government programs will be created in the future because of the effects from this virus? These and a thousand more questions will have to be dealt with down the road.

Summary

These are troubling times, full of concern and worry. We kindly ask that you focus on setting up a routine of positive distractions. Do whatever you need to do to increase your emotional competence and get your health and spirit through this ordeal.

Robert Hopkins, one of the most loyal aids to FDR loved telling the following story. Hopkins was riding in the back seat of a convertible with FDR. They were driving to meet FDR's mother, Sara, in New York. Sirens blared and lights flashed from their police escort and Secret Service detail. Sara met the group out front. When she saw FDR, she admonished him for not wearing a sweater. FDR tried to change the subject, but Sara insisted right then and there that he put on a sweater on. Sara did not care that the public, the police or the Secret Service were watching. Sara was simply taking care of the most powerful man in the world who was still her cherished son.

We feel the same about caring for you and your financial situation at this time. We will get your money through this difficult period. Please take care of yourself, your family and your friends.

You have a team of seasoned problem-solvers focused on the issues the of the day. It brings everyone at Cal Cap great comfort to know we planned, prepared and practiced for these chaotic moments. We hope it brings you comfort too.

Winston Churchill said during a despairing moment of WWII, "If you're going through hell, keep going." What he did not say, I will say now. Hell brings opportunities, which is the focus of the note you will receive next week. Thank for your trust and confidence.