Weekly Capital Market Comments

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NORTHEAST SEQUOIA
PRIVATE CLIENT GROUP

Raking Leaves In The Wind

The best way we can describe the current market backdrop, is to compare it to raking leaves (yes, some of us still do it) on a windy autumn day. As you rake in one direction, all too often, the wind blows all your hard work in the other, leaving you frustrated and close to ceding victory to Mother Nature. But you persevere. Now you believe that your 2.0 horsepower (200 mph) leaf-blower can do the trick, but this just proves to be utterly useless as you are now getting scowling looks from your neighbor, as you jettison leaves on to his front lawn or worse yet…into your wife's flower beds. Then…you finally abandon all hope of progress…until the wind dies down.

This is where we are today. As we pointed out in our 2020 Outlook, 2019 was the year of the "everything rally." However, the last four weeks have proven to be a period whereby cross-asset volatility has increased significantly, pushing valuations to levels as irrationally low, as they were unreasonably high just a month ago. Few asset classes have been immune from the perfect storm caused by a global pandemic, topping-out of economic data, and a turf-war for oil production and pricing. Even gold, while outperforming most other asset classes, has sold off, as have municipal bonds. Liquidity concerns have resulted in forced selling. Even the 10Y US Treasury has sold off during the last week, as yields backed up from the lowest levels in history.

The rub now is trying to determine if and when it is time to reverse course and bolt risk back on to your portfolio. Perhaps the best technical analysts we follow said it best, ***"…a bottom is a process, not a price."*** Meaning, that we need to witness a series of events, all in concert, to help comfort the notion that downside guardrails are forming.

So what are we looking at now, and how are we communicating with clients?

1. First and foremost, we reiterate the notion that a bottom is a process, not a price. Unfortunately, the signposts that signal this bottoming process will not be pleasant to monitor.
2. We will first need to see unemployment skyrocket and claims rise to levels never thought imaginable. We will need GDP to plummet, and almost every other economic data point (PMIs, retail sales, auto sales, small business sentiment, and consumer sentiment) that we monitor move to a DEFCON 1 or 2 level.
3. A general social panic sets in, people become frozen from doing normal daily activities.
4. We will cringe, as the main-street economy goes out of business for four to six weeks.
5. Markets will observe extreme market volatility, in a manner not reflective of underlying business fundamentals.
6. We need to witness a freeze in credit markets; then for central bankers across the globe to slash rates and once again enact unorthodox liquidity measures to grease the cogs of the banking system, so that liquidity will be provided to creditworthy business.
7. **Finally, we will also listen to talking heads warn that this is only the beginning.** These are the same folks suggesting at 19x forward earnings, that market and earnings fundamentals were primed to push the S&P well above 3,400.

So when we review this list, we can begin to check-off a number of our signposts. At the same time, we are not sounding the all-clear just yet. In our March 2, 2020, Weekly entitled, "Fashionably Late Or Dimwittedly Early?" we suggested that we'd rather be late to a great party, than early to a dud. This is a position we still hold. But we warn our clients that the economy will get worse before it gets better, and the medical emergency will become direr before it flattens out. At the same time, markets disintermediate, discount, and overshoot. We are actively looking at ways and opportunities to benefit from this. We just need the wind to die down for a little bit. **We'd love to hear your thoughts.**