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Market Update: April 26, 2020

Global stock markets were down less than 2% for the week. The week included some very challenging economic news along with a collapse in oil prices. Also, let's not forget that the previous two-week rally was the strongest since the 1930s. When you add it all up, maybe the markets are showing surprising resilience in the face of this pandemic.

> **The strong rally in equity markets suggests that investors have been more focused on the spread of COVID-19, and less focused on the fundamental data. This may also suggest that investors are simply looking past the bad fundamental data that is expected over the next few months and focusing more on what comes after the COVID-19 pandemic.**

J.P. Morgan Asset Management – Market Insights 4/20/20

Stock valuations don't really matter much in a coronavirus world. Reported earnings for the first quarter are even less relevant, because two of the months were pre-COVID-19.

> **Valuation analysis is proving to be a somewhat-futile task.**

Liz Ann Sonders – Charles Schwab Investment Mgt 4/20/20

J.P. Morgan Asset Management expects S&P 500 profits to contract over 14% in the first quarter. Sectors sensitive to social distancing will get hit the hardest, while companies that are somewhat insulated or positioned to benefit from the stay-at-home economy will fare better.

> **The markets completely lack direction. There's just no ground on which to anchor your forecasts because the size of this shock is completely unknown.**

Agnes Belaisch, Barings Investment Institute – WSJ 4/23/20

Oil futures went negative on Monday, highlighting the extreme stress in oil markets due to declining demand and limited storage capacity. Monday was the last day traders could sell the May 2020 WTI (West Texas Intermediate) futures contract … and avoid taking delivery on oil that had no place to be stored. Oil prices currently trade well below levels that make it profitable for most companies to produce.

> **Oil is really the big gorilla out there in the market right now because of the dramatic actions. The bigger picture is not just the near-term impact but the longer term, the ultimate solvency of these companies and the potential impact on both their stocks and their bonds.**

Lisa Erickson, U.S. Bank – WSJ 4/22/20

Infrastructure for storage and delivery has not kept pace with the shale oil boom that has made the U.S. the world's top oil producer. Refineries, storage facilities, pipelines and ocean tankers are at or near capacity, while the world economy remains at a relative standstill.

> **If nobody wants to refine oil now, and if you can't store crude for when people want it later, the fair value of any additional crude you pump out of the ground has to be less than zero.**

Matthew Klein – Barron's 4/20/20

Nobody thinks this is a permanent condition. But for now, demand is declining much faster than supply.

> **This is a market signaling to producers that you need to cut off more production faster because we're drowning in oil at this point.**

Saad Rahim, Trafigura economist – WSJ 4/21/20

On Thursday, Congress passed legislation that provides $484 billion of stimulus to support small businesses, aid hospitals, and increase

resources for coronavirus testing. The bill funds $310 billion more for the Paycheck Protection Program, which exhausted its initial $350 billion allocation last week. The bill also provides for $75 billion to hospitals experiencing budget constraints during the pandemic.

> **Unemployment and deflation are the clear and present problems. But the unprecedented fiscal and monetary policy, plus the effects of a continued retreat from globalization, eventually could lift inflation.**
>
> **Randall W. Forsyth – Barron's 4/24/20**

The Labor Department reported that over 4 million Americans applied for unemployment benefits during the week ended April 18. Although the headline number was dreadful, it was consistent with expectations and represented a decrease from the previous week. That brings the total claims for the past five weeks to over 26 million.

> **The key is we're now looking at the reopening of the U.S. economy and the assumption that when it reopens, these claims will start to reverse themselves. This is going to be a very uneven gradual process.**
>
> **Peter Boockvar, Bleakley Advisory Group – WSJ 4/23/20**

States are running out of funds to cover the millions of laid-off workers who applied for unemployment-insurance benefits. The cash squeeze comes at a time when states are facing additional coronavirus costs and declining revenues from their stalled economies. No state has run out of money, but at this point it seems inevitable for many.

> **To the extent that their own reserves are running low, they have the ability to take an interest-free loan up from the Treasury. It wouldn't surprise me to see more avail themselves of that going forward.**
>
> **Eugene Scalia, U.S. Labor Secretary – WSJ 4/20/20**

Business activity in the U.S., Europe, and Japan has collapsed according to Purchasing Managers Index (PMI) surveys. The surveys suggest the global economy has almost certainly entered a recession. The global decline that's happening now in services-sector activity – where face-to-face interaction is unavoidable – is unprecedented in the history of such surveys.

> **While we knew lockdowns were shutting down large parts of the economy and expected the PMIs to decline from March, the scale of the falls in today's release was staggering.**
>
> **Rosie Colthorpe, Oxford Economics – WSJ 4/23/20**

Back in 2019, the International Monetary Fund estimated that 40% of Africa's low-income countries were experiencing debt distress. Declining commodity prices, in addition to the pandemic induced slowdown, are making it all but impossible to service their debt.

Africa's poverty-stricken economies are now looking for some debt relief, and their largest creditor is China. China is known to use indebtedness of weaker neighbors to gain leverage and pursue strategic objectives. A Harvard Business Review study suggests that 50% of China's loans to developing countries goes unreported.

The debt to China, estimated at nearly $150 billion, was used to finance large-scale infrastructure projects. This is part of China's Belt and Road Initiative, which requires borrowers to give the Chinese *seller preference* in spending loan proceeds, and contains provisions that would force borrowers to surrender state assets if they default.

> **Wealthy countries from the U.S. to Japan – watching their own economies lurch toward recession – are loath to forgive African debt if they think the money will indirectly support Chinese creditors, including the government, banks and contractors.**
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> **Parkinson/Areddy/Bariyo – WSJ 4/17/20**

How long can the U.S. economy remain closed? We know the current shutdown is not sustainable, but reopening too quickly can introduce a host of uncertainties and expanded risks.

Matthew Harrison, head of biotech research at Morgan Stanley, suggests these four major components are needed to ensure a sustainable reopening:

1. Adequate surge capacity in hospitals
2. Infrastructure to support testing
3. Robust contact tracing
4. Widespread access to serology testing (to determine who might be immune to the virus)

> **In the long run, though, there are really no compromises between fighting the pandemic and preserving the health of the U.S. economy and financial markets … Pandemics depress economies, but public health interventions don't. Such interventions instead can lead to both better economic outcomes and lower mortality rates.**
>
> **Lisa Beilfuss – Barron's 4/23/20**

To put those four components in place suggests that April and May would be the low points … and we could start to turn things around by June. Either way, this quarter is shaping up to deliver the worst economic results we may ever experience in our lifetimes.

> **We've had this incredible rebound, but I think we're going to see a second wave of weakness as people take in what these economic figures mean.**
>
> **Altaf Kassam, State Street Global Advisors – WSJ 4/23/20**

Consider the recent performance of U.S. stocks. They were down 15% in the fourth quarter of 2018, up 30% in 2019, up over 5% through February 19 of 2020, down 35% from February 19 through March 23, and now up 27% from March 23 to April 24. Believe it or not, performance over this entire period ended basically flat.

All investors want to *buy low and sell high*. However, reacting to volatility will inevitably cause investors to buy into rising markets and sell into declines. Anyone trying to time the markets over the past 18 months or so probably got hurt.

Being humble and staying disciplined is more important than ever for investors. Stay safe, and let us know if we can be of any help.

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