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Market Commentary

Covid-19 Containment in Asia May Show the Path to U.S. Market Recovery

Continuing uncertainty over the coronavirus pandemic caused all major asset classes — stocks, bonds and commodities — to fall simultaneously, effectively leaving investors with no safe haven. This occurred despite the Fed's ongoing actions to expand liquidity and the federal government's plan for massive fiscal spending. After a 5.2% decline on Wednesday, the S&P 500 is now down about 30 percent from its all-time highs on February 19.

There is clear evidence of panic selling as many investors fled to cash. Amid the extreme volatility, clients frequently ask how low can the markets go and how bad can the financial situation become. The honest answer: No one knows. We suspect financial markets are closer to a bottom, but the medical-based nature of this crisis, combined with panic selling, makes it difficult to pinpoint the exact price or timing for a bottom.

The causes of the current bear market are fundamentally different than past bear markets. This is a health crisis that is straining the economy and markets — not a financial crisis like 2008 with structural financial system weakness that prolonged the recovery. Instead, current market weakness is a reaction to fear of the unknown and the potential economic impact of efforts to contain the virus — quarantining consumers, closing non-essential businesses and effectively shutting down auto manufacturing. Investors' fears and the economic impacts are real, but are also more likely to prove transitory over time.

The second source of concern — the disruptive containment efforts — are ironically the most effective current solution to stop the infection and lead to a recovery. The experience in China, Japan and South Korea shows the efficacy of their containment efforts, with clear peaks and declines in the number of new cases within their borders. In each country, it appears the markets took notice, outperforming broad global markets shortly following the peak in the number of new cases.

Of course, these countries had previous experience with containing pandemics, such as the 2003 SARS outbreak, and thus had a relatively well-developed playbook that could be implemented quickly. Although the U.S. and European countries have advanced medical systems, they have had less experience in responding to pandemics and have exhibited slower reactions to contain the coronavirus. In the U.S., the outbreak was delayed for weeks after it began spreading in Asia, and so broad-based containment efforts have only recently begun. As a result, it would be reasonable to expect the growth of the pandemic to continue in the near-term, until the containment efforts can have an impact.

We are encouraged that governments continue to deliver monetary and fiscal stimulus to provide an economic and financial backstop during this crisis, but signs of success in containing the virus, similar to those in Asia, will likely be needed to instill confidence in a recovery.

As a result, it is difficult to predict when the number of new infections will peak in the U.S. or when our financial markets may begin to recover. Nonetheless, we believe investors should stay the course, rather than try to pick the bottom. The U.S. stock market's near-30% decline means that equities are moving closer to a bottom and are now more reasonably priced, creating a prospective risk/reward that may be more favorable for long-term investors. Past bear markets have generally been followed by recoveries within 12 months. Further, the unusual nature of this crisis — medical and not economic — creates uncertainty, although we think it is likely to be transitory. This should provide reason to be optimistic about the market's eventual recovery.