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Market Commentary
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Introduction

Fear from the spread of coronavirus rattled markets in the first quarter of 2020 resulting in panic selling across asset classes and levels of volatility not seen since the 2008 global financial crisis. The total number of confirmed coronavirus cases has increased, resulting in a partially sick workforce and "social distancing" rules put in place by lawmakers to help contain the virus. It is expected that there will be less economic activity over the short-term as a result of all of this. More recent economic data points have already proven a slowdown is well under way. While this is all true, it should not be forgotten that economic data was not all that bad prior to coronavirus taking its toll on the economy. The unemployment rate as of February was low at 3.5%, GDP remained positive in Q4 of 2019 up an annualized 2.1%, and inflation as measured by CPI was not concerning up 2.3% on a year-over-year basis. Another positive sign is that the Federal Reserve has showed tremendous support by cutting the Federal Funds target rate to nearly 0% and stating that they would act as a buyer or lender of assets to keep the economy afloat while it is on pause. The U.S. Government has showed massive support as well, recently approving the CARES Act, which is the largest fiscal stimulus package in U.S. history, with an estimated amount of $2.2 trillion in aid going to areas such as the unemployment system, small businesses and our healthcare system. While things may get worse before they get better, a strong consumer prior to the outbreak, pent up demand after this is over and historic monetary and fiscal packages in place today lead us to believe there will be a sharp recovery by year-end.

Domestic Equities

U.S. stocks posted their worst quarter since the 2008 financial crisis with the S&P 500 declining -19.60%. The bulk of the first quarter's negative performance came in March when the index was down -12.35% as the spread of coronavirus started to accelerate exponentially in the U.S. Coming into the year, valuations for U.S. stocks looked expensive relative to history off the back of substantial price appreciation for stocks in 2019 combined with low single digit earnings growth projected for 2020. While higher valuations may have been partially justified by a healthy consumer, lower borrowing costs, manageable inflation and a phase 1 trade agreement, news regarding the spread of coronavirus was enough to tip the scale and send stock prices plummeting. Riskier, smaller sized companies were disproportionately affected by the panic selling that occurred in the market with the Russell 2000 index down -30.61%. With expectations that volatility will persist over the next few months as the virus impacts U.S. businesses, we believe the market may be poised for a sharp recovery as valuations look more attractive today than they did at the start of the year and financial assistance provided by government can help bridge the gap for U.S. companies until the economy opens up once again.

International Equities

International developed equities and emerging market equities returned -22.83% and -23.60% for the first quarter, respectively, both lagging the S&P 500. Foreign equities were hit hard as many international economies came to a halt due to the outbreak of the coronavirus, with countries like Italy and Spain even announcing full or partial lockdowns. As the globe continues to battle the outbreak, downside risks surrounding slowing global economic growth persist. Governments and central banks around the world have shown a willingness to step in to support their economies, with the European Central Bank announcing an $818 billion-euro asset purchasing program that will extend through 2020 and possibly beyond. The Bank of England also announced that it would cut its benchmark interest rate to a record low of 0.1%, as well as an asset purchase program of $232 billion worth of U.K. government bonds. Global GDP is now expected to grow at half the forecasted rate in 2020, with many developed nations likely falling into recession.

Within emerging markets, the trade tension between the U.S. and China that weighed on major emerging market economies such as China and other Asian countries has become an afterthought to the pandemic. Despite being the origin of the outbreak, it appears that China is poised to reach a recovery this year, with China's Manufacturing Purchasing Managers Index (PMI) rising to 52.0 in March, up from 35.7 in February, and the Non-Manufacturing PMI (services sector) rising to 52.3, up from 29.6 in February. The collapse in energy prices due to the price war between Saudi Arabia and Russia has also put pressure on emerging market economies such as oil exporters from certain Latin America and Middle East countries.

Fixed Income

The fixed income market, as measured by the Bloomberg Barclays US Aggregate Bond index, returned 3.15% in the first quarter due to the index's treasury exposure, however, corporate bonds were punished from an overwhelming risk-off sentiment in financial markets. In response to the stress in financial markets, the Federal Reserve took extraordinary action over the past quarter by cutting rates to zero and announcing that they would purchase an unlimited amount of treasury and mortgage backed securities in order to restore stability in these markets, as well as a number of lending facilities to restore order to credit markets. As a result of a flight to quality and decreasing interest rates, demand for longer duration securities increased and pushed yields down, with the 10-year U.S. Treasury yield ending the quarter at 0.66%, a drop of 1.26% from the beginning of the year. As both short and long-term rates came down during the quarter, the difference between long and short-term rates widened to as much as 0.68%. We believe the projected path for interest rates will remain stationary, as the Federal Reserve has little incentive to lower rates below zero in addition to the extraordinary measures they are already undertaking to restore order to financial markets. Moving forward, we believe fixed income securities will provide significant diversification benefits to equities as economic and corporate growth slows.

Alternatives

Alternative asset classes fell along with equity markets to start the year. Plummeting demand from coronavirus disruptions coupled with a relentless price war between Saudi Arabia and Russia drove oil prices to multi-decade lows. On March 30th U.S. crude oil touched $19.27 a barrel, the weakest intraday price since February 2002. U.S. crude ended the first quarter of 2020 only slightly higher at $20.48 per barrel down from $61.18 per barrel at the beginning of the year. Hedge Fund like alternatives failed to protect investors given the extreme volatility in the market as exemplified by the Morningstar Diversified Alternative index which ended the quarter with a return of -13.82%.

Real Estate

The housing sector was poised for solid growth in 2020 as historically cheap borrowing costs, high consumer confidence, and a tight labor market led to increased housing demand. As with other areas of the economy, the coronavirus has adversely affected the housing market and slower growth is expected in the months ahead. The most recent data is mixed and underscores the previous strength in the sector. Residential starts fell -1.5% in March to a 1.599 million annualized rate, although, higher than the expected reading of 1.5 million. Building permits, fell -5.5% to a 1.464 million annualized rate in March. Upcoming data for April should be more indicative of a housing market and economy that has been shut down due to biological concerns.

Conclusion

It is no surprise that the U.S. economy has been put on halt as the world tries to recover from the novel coronavirus. Many have tried to compare our current economic situation with the 2008 financial crisis but the reality is they are nothing alike as 2008 was a crisis in our financial system versus today where we have a health crisis that has significant economic consequences. While we take today's coronavirus pandemic seriously, we do believe there is a light at the end of the tunnel. Over the next few months we expect volatility to persist as market participants make sense of poor economic data releases and there are a larger number of confirmed coronavirus cases. Although the timeline to recovery is unknown, we do believe the number of active cases here in the U.S. should eventually plateau, leading to a recovery in the economy and potential for upside return for investors.