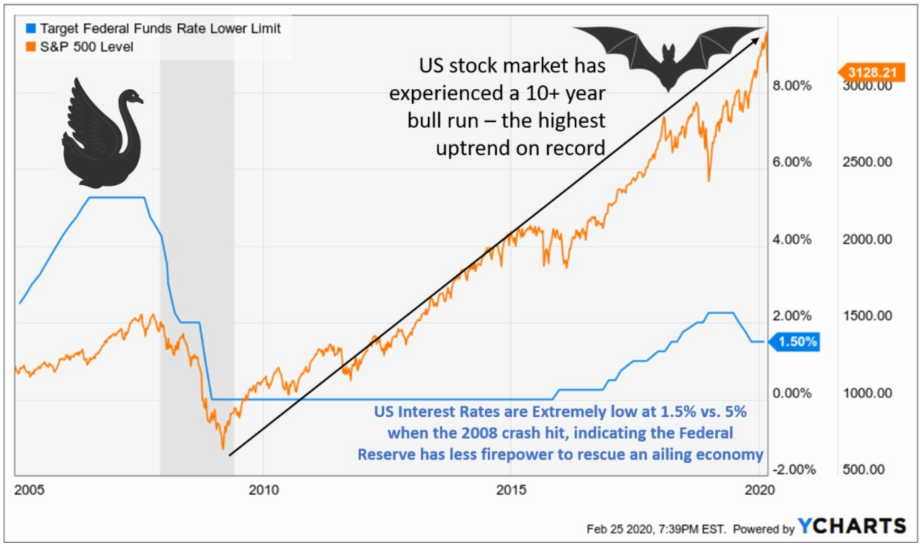
Invest Wisely©

Greetings!

Last month, I warned in my newsletter that the Coronavirus (COVID-19) could be a Black Swan event that threatened to precipitate a significant market crash, which I called the Black Bat Market Crash.[1] I coined the phrase "Better to Be Safe than SARSy" and advised that investors should consider taking profits from the 10+ year bull market. Had you taken my advice, you would have saved yourself 24% in the stock market (see table 1 below). Even bond funds were negative as I warned in *The Wall Street Journal*.[2] Cash is queen. Had you been my client, you would have saved even more as I was taking profits for my clients at the stock market peak the week before. Based on analysis of the dot com and 2008 financial crisis (detailed below), we cannot rule out another 25% drop in the market and investors should protect their portfolio or their psyche for this possibility. If markets are to fall another 25% and you were to sell out of equities now into cash, you could save yourself over 4 years on average trying to get back to today's value (see analysis below). If you want to stay invested in the market, the Coronavirus is having a transformative effect to the global economy and strategically picking sectors and companies is likely to outperform the broader market and may even gain positive returns. I've now constructed a Coronavirus Portfolio for my clients which aims to make money in this environment.

When I sent out my email on Feb 26, I received pushback from some of my readers who sent reports from Goldman Sachs and other firms which minimized the economic impact of the COVID-19. Goldman showed that the market had continued to perform well during other viruses like SARS, Ebola, and the swine flu.[3] These epidemics are not comparable as they took place in economic backwaters - small rural villages without much global trade, had short incubation periods, and were less contagious. When SARS first emerged in 2003, China had just joined the WTO and a virus in a Chinese rural community had little impact on the world economy -- especially as the US housing market and economic recovery was gaining steam after the dot com crash. Now, China is an economic superpower and Wuhan has global trade ties and we can see the rapid global spread of the new SARS virus, Goldman Sachs analysts changed their tune and have now warned of a global recession.[4]

US Stock Market Is Vulnerable Given a 10 Year Bull Market, and Historically Low Interest Rates



Global governments and people around the world have decided that "It's Better to Be Safe than SARSy" with respect to their health. Countries across the world including Italy, France, Germany, and the US have to varying degrees locked their borders, closed schools, banned restaurants from staying open, and demanded people lockdown in their homes for all but essential trips.

These lockdowns will have a gigantic effect on the local and global economies not just for the near term, but for the future. Restauranteur Tom Colliccio declared this a World War II moment and estimated that 75% of independent restaurants may not re-open after this crisis.[5] Discretionary retailers who were already on the brink of bankruptcy due to Amazon and high rents, may see the coronavirus as the nail in the coffin of their businesses.

Some pundits like Scott Minerd of Guggenheim have acknowledged this massive impact on the global economy and has issued a 10-20% call for a DEPRESSION, not even a great recession.[6] Yet, it seems like the vast majority of pundits quoted on CNBC and in the financial press are still minimizing the impact of the COVID-19 and they are advising clients to either stay fully invested in the stock markets and to start buying on the dips.

Table 1: Comparing the Current Market to the Past Two Market Crashes

Dot Com Crash	Date	S&P 500 Level	% down from Peak
Pre-crash Peak	3/24/2000	1528	0
Day before 9/11	9/10/2001	1093	-40%
Trough	10/9/2002	777	-49%
Back to peak	5/31/2007	1531	
# of years from trough back to peak			*7+ years*

2008 Financial Crash	Date	S&P 500 Level	% down from Peak
Peak	10/9/2007	1565	0
Trough	3/9/2009	677	-57%
Back to peak	3/28/2013	1569	
# of years from trough back to peak			*5.5 years*

Black Bat Market Crash	Date	S&P 500 Level	% down from Peak
Peak	2/19/2020	3386	0
Black Bat warning	2/26/2020	3116	-8%
Most recent close	3/20/2020	2305	-32%
Average loss of 2 last crises			*-53%*
Average number of years to recover:			*6-7 years*

Source: Maya Joelson, ycharts data.

As you can see in the table above, the S&P 500 fell 49% from peak to trough during the dot com crash – this was exacerbated by 9/11 terrorist attacks. But, the market had already fallen 40% from its dot com peak until the day before the surprise attacks. It took over 7 years for US stock market investors to regain the money they had held at the peak of the dot com boom. Likewise, the 2008 financial crisis resulted in a 57% fall from peak to trough and took 5.5 years to recover. If you think the impact of the Coronavirus will have a comparable impact to the economy and the markets, the stock market could fall another 24% on average. While some people do not believe in market timing, some may believe it is better to be safe than SARSy. Selling now could save you a lot of time in investment years. We may even be able to make money by selling out of broad indexes and mutual funds and repositioning and strategically picking new, relevant stocks for this Coronavirus environment.

A few things to consider.

1) Market Timing and Known Unknowns. While many say it is difficult to time the market, I refer to Donald Rumsfeld's analytic framework of "known unknowns".[7] We know the coronavirus is forcing closure and severe economic consequences on many industries, people, and businesses across the globe. Unknown is how long the virus will persist and pervade our lives. On the flip side, the US government is talking about fiscal and monetary support. I think your life savings are worthwhile to weigh up what you think is the overall net effect to make a calculated decision about whether and how you want to invest in the market. The market timing speaks of long-term averages but in the short-term, we have concrete decisions to make based on the current plausible scenarios. I used to run macroeconomic scenario analysis for the global mining firm Rio Tinto after they realized it was critical to their solvency after the global financial crisis. Scenario analysis is also critical for you to prepare for the range of outcomes.

2) Percent Losses are More Potent than Percent Gains. It might be easy to see the market down 7% one day, and up 7% the next day and claim that the market has bounced back. But this denies basic math. If you lose 50% of your money, you will need to double or gain 100% to get back to even. A lot of analyses I have seen show the gains from the trough – for instance had you invested since March 2009 – but ignore the amount of principal lost by staying invested through the -57% Great Recession peak to trough decline. If you lose 25% of your money, your portfolio would have to grow by 33% to get back to start. As average annual market returns are 8%, this means it would take over 4 years on average to get back today's principal.

3) Warren Buffet's Naked Swimming Analogy - Are There Other Issues Like a Credit Crisis that Might Domino? Warren Buffet is famously known for stating that, "You only find out who is swimming naked when the tide goes out."[8] The all but essential halt of economic activity may surface problems that were not clear when the market was booming. For instance, years of cheap debit and sudden recession may show that many companies and countries have only been able to survive through cheap debt. This could create knock-on effects to their banks and the equity and credit markets. Defaults and bankruptcies could domino.

4) Panic-Selling vs. Preparing for a Threat. Some investment advisors advise clients not to panic-sell. Yet, if you have new evidence, that there is a threat that may burn your house down, shouldn't you prepare and evaluate your plan and strategy? It is better to prepare for a downfall, instead of ignoring it. What if this was the Titanic - when would you get off?

5) Ability of the World to Respond and Stimulate the Economies. As stated in my Black Bat Crash paper, sovereign governments around the world seem to have fewer bullets with which to address economic distress and to get a recovery going. US interest rates have fallen below 1% and cannot be reduced much further to stimulate the US economy. The 2001 dot com crash revived in part by a booming housing market which was stimulated by lower interest rates. In response to the 2008 crisis, China launched huge infrastructure spending which helped spur emerging markets around the world.

World leaders and people around the world have decided that it's "Better to Be Safe than SARSy" with respect to their health. I think investors should take the time to consider their situation, risk tolerance, and weigh the upsides and downsides with respect to their life savings. Some of my clients wanted to take all of their savings off the table, particularly in retirement accounts, and have been well-served. Other clients were concerned about capital gains so I analyzed their holdings and sold strategically and bought new stocks to reposition their portfolio for this new Coronavirus future. In fact, there are many companies that are playing pivotal roles in this time and their stocks have benefitted. But the overall equity market is full of industries such as airlines, hotels, energy, discretionary retail, and financials that are likely to suffer in this market. This may be the time that shows that strategic investing and stock-picking is the best way forward.

If you decide to stay the course, I respect that. In your interest, I wanted to lay out some of the downside risks for you to consider if the market impact is similar to the last two recessions. Many analysts have also warned of a potential depression, which would be even more dire and you would benefit even more from repositioning your portfolio.

When it comes to analyzing your life savings, it is better to be safe than SARSy.

Please feel free to reach out to me to discuss your situation and provide any feedback on this newsletter. Please also forward to friends, colleagues, and relatives who may find this perspective useful.

Best regards and stay safe!
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Maya is a Harvard-trained economist who leverages her two decades of top-level experience across Wall Street, the City of London, emerging markets, and advanced technology to devise investment strategies for her clients. She advised the CEO and Board of Rio Tinto on macroeconomic and geopolitical concerns. Maya founded Meta Point Advisors after

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Marisa Joelson holds a MPA from Harvard Kennedy School, a MBA from Kellogg at Northwestern University, and a BA from Wesleyan University.

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