QUARTERLY MARKET COMMENTARY: 2020-Q1

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After hitting all-time highs in February, U.S. equity markets abruptly turned for the worst as discerning news emerged regarding the novel coronavirus. In over a month, the Dow Jones Industrial Average (DJIA) dropped from a record high of 29,500+, to a 52-week low of 18,200+, before recovering almost 3,800 points, or 20%, to close out the first quarter at approximately 22,000. Despite experiencing daily volatility that was so extreme and unnerving, client portfolios held up relatively well on a year-to-date basis. However, we did note that a typical balanced portfolio would have experienced stronger performance had certain classes of fixed-income investments not come under pressure due to the realities of the economic shutdown. The shutdown has reached beyond corporate earnings and has created a dangerous threat to cash flow, which supports distributions, interest payments and dividends.

During the performance attribution process, we observed how the negative impact on fixed-income (conservative) investments within client portfolios reduced the effectiveness of the asset allocation decision in mitigating downside risk. How we move forward is predicated on a similar experience in 2013 when fixed-income investments dragged overall portfolio returns due to rising interest rates in what was perceived as an accelerating economy with rising inflation. It turned out that this was not the case and interest rates went back down resulting in a recovery in bond prices. Consistent with our approach in 2013, we will continue to hold existing income generating vehicles believing that Real Estate Investment Trusts (REIT's), corporate bonds, municipal bonds and preferred stocks will fully recover upon a restart of the economy. Expectations for equity like returns from the recent lows are not out of the question as we recall the recovery from the Financial Crisis.

Another note from our evaluation of portfolio results involves the use of defensive equities in mitigating downside risk. Value, or dividend yielding stocks, that are normally safe-haven favorites surprisingly faltered during the recent crisis. This can be attributed to specific sectors and companies whose dividends are being threatened by the current economic shutdown. Our approach for these sectors and companies will be consistent with our hold on fixed-income investments. However, we believe the recovery for the latter will be more immediate when economic conditions return to normal. In conclusion, the only component in our three-prong approach that held up to expectations in mitigating downside risk is the cash decision. Despite falling rates on money funds, cash has become an extremely important asset class in holding up portfolio values in addition to minimizing sequence risk.

Since the last commentary, we have already made two downward revisions to our 2020 DJIA target. The first adjustment reflected a scenario presented by Goldman Sachs where there is 0% earnings growth for the current fiscal year. Now that we anticipate a negative earnings growth scenario for 2020, our updated target range based on fundamentals is currently between 23,800 and 25,700. Even as we provide updates to our DJIA target, we realize this may not be meaningful due to too many moving parts in this unique market environment. Skepticism can also exist when monitoring actual economic reports that come out during the second quarter. We believe we do not need actual numbers to tell us how bad the quarter is because we have already accepted the fact that this will be an unremarkable quarter, to put it kindly.

Even though we have recently experienced a technical rebound in equity markets, the challenges we face will not be resolved overnight. Volatility will be with us as we continue to monitor near-term factors such as monetary & fiscal policies, COVID-19 data and additional news on possible medical breakthroughs. We will continue to make portfolio decisions for the long-term, looking beyond 2020. In closing, we truly appreciate our clients who have reached out to us to check on our well being as well as expressing their confidence in our ability to help them navigate through such difficult times. You are the reason why we do what we do. We continue to move forward with patience, fortitude and prayer as we hope you and your family stays safe during these unprecedented times!