MARKET RECAP

MARCH 31ST, 2020

MARCH 2020

HISTORIC STOCK DECLINES, RECORD LOW 10-YR YLD. FED CUT TWICE, RECORD STIMULUS.

A month not to be repeated. The fastest free-fall in US equity markets, the S&P 500 declined 20% in 20 days (Dow more, the Nasdaq less). Monthly losses ran double-digits even with a final week rally. Outflows beget outflows in every asset class, with equity markets hardest hit. The benchmark index opened the month in correction mode, a loss of more than ten-percent. That doubled before mid-month dropping the S&P into bear market, the first in eleven years. The longest and second best in total returns. In simple numbers, 676 became 3386, a five-fold increase. The drop was more sudden, the fastest ever, and the 12th bear market since WWII.

The second-half saw the worst week since the final week in February, and both weeks were the worst since October 2008. Strong statement. Twice, the Fed cut the overnight funds rate, but both were properly labeled 'emergency' rate cuts, neither lifted stocks, both times equity markets were pummeled, declining by large absolute numbers 'and' in percentage terms too.

Finally, as fiscal policy was about to join the fight to rescue the economy, a three-day rally in the midst of the gloom helped stabilize markets, at least for now. However, despite the rebound, outflows in equities continued unabated last week, the scale remained high (ditto in most asset classes), and so fair to see the initial wave was mostly a function of short-sellers covering previous positions. Will a second wave emerge, buyers viewing valuations and prices attractive enough to add/rebalance existing portfolio positions? An important question to be answered the next few weeks. From opening bell, the lion never became a lamb. In the end, this bull market 'unofficially' – started and finished in March – 11 years apart.

Also, the third month on the calendar will be remembered as the starting point of a new recession. Beyond the technical definition of at least consecutive negative quarters, there is the official more encompassing description which includes a general decline in economic activity, with employment, industrial production, productivity and stock market prices all playing a role in the official classification of a downturn being labeled a recession. That appears a formality, and fully-discounted by markets (bonds and stocks). The more intriguing uncertainty is the length of this downturn. Approximately two quarters or longer? In relative terms to 2008, consensus does not see anywhere near the 20-month recession endured then, but the steepness of the fall is quicker as well as the respective monetary and the fiscal responses this month. The Fed's acrobatic announcements came in lightning order, sometimes daily, while congress worked at warped-speed.

A short summary of credit and commodities follow. In fixed income, anything that was not a Treasury bond lost value, and in many cases, losses totaled double-digits. From taxable to tax-exempt, record outflows were recorded. Outflows hit a high point in the second-half, before a series of steps by the central bank added sufficient liquidity to calm the upper-class of credit – investment grade bonds (IG spreads reached 360 bps over USTs, narrowed to approx. 290 by the end of last week). Spreads on high-yield debt touched distressed levels before paring losses ahead of month-end. Municipals saw differentials to Treasuries reach all-time wide levels, further-out than in 2008. In short, the true safe-haven remains the Treasury market. Before and after the Fed's twin rate reductions, the yield on the 10-year note dropped steadily at first then cascaded down. The benchmark note dropped below 1.3%, the old record by the end of February, kept hedging south, through the 1% barrier, all the way to near 0.3% on a day (though not the only one) where panic set-in. That day saw the yield cut in more than half. Further-out, a few days later, the yield rebounded back to 1.2%. In other words, almost a round-trip. Finally, lower again, below the psychological 1% mark. In the final week yields were beginning (attempting) to stabilize. Not there yet, but some signs to that effect.

As for commodities, there was no rollercoaster, no circle-eights, just a one-way ticket down the barrel. WTI dropped to $20 from $45, a humongous percentage drop in one-month, and the lowest actual price in nearly two decades. A perfect storm from all angles and directions, economic and political. Early in March, the three-year cooperation between Saudi Arabia and Russia was fully expected to continue, with a further reduction in production to reduce global oil supplies. But the emergency meeting produced no meeting of the minds, quite the opposite. A price war ensued, and over a weekend, the price of a barrel dropped more than 30%. That proved to be a second catalyst for financial markets in general and the dominant factor for a historic decline in oil prices.

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INVESTOR SPOTLIGHT

START OF Q2: THE ACTUAL COUNT. DOES APRIL SEE THE DESIRED FLATTENING OF THE VIRUS' CURVE? IF NOT, IS WORST-CASE SCENARIO ON THE ECONOMY FACTORED-IN? CREDIT MARKETS: SHORT-TERM, FOCUS ON SPREADS…SPEAKING OF, THE '*TED SPREAD'* (DIFFERENTIAL BETWEEN 3-MONTH T-BILL AND 3-MONTH LIBOR). IN NORMAL TIMES, THE SPREAD IS RELATIVELY NARROW; WIDENED SIGNIFICANTLY IN MARCH. WHETHER IT'S STOCKS OR BONDS, WHEN DO OUTFLOWS TURN TO INFLOWS? WILL THE U.S. DOLLAR FLATTEN-OUT? LIQUIDITY STRESSES WERE ADDRESSED BY THE FED…WAS IT ENOUGH? HOW ABOUT DAILY / WEEKLY REPOS? BEFORE CRISIS, THE END DATE WAS SET FOR MID-APRIL. HOW FAR INTO THE FUTURE? FED'S BALANCE SHEET?

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