

## Our Perspective on These Unsettling Times:

**Over the weekend, the Federal Reserve lowered its key interest rate a full percentage point to near 0%.** They also committed to buying \$700 billion in Treasury securities. While these measures are supportive of markets, the reaction today was unable to stave off investor fears. As we await the Congressional Emergency Coronavirus Bill which is slated for a vote this week, individual states are taking measures to limit contact by closing schools and limiting businesses operations or hours. Greater Federal assistance both financially, even perhaps militarily, are possibilities that could help in the response.

**It is important to keep in mind that this is not the first time that the United States has been hit with an external shock, grinding many parts of its economy to a halt.** In our most recent past, we remember images of the World Trade Center towers after the two hijacked airplanes struck the towers on September 11, 2001. The response by the Department of Transportation was to close the National Airspace for two days. The New York Stock Exchange closed for 4 days and downtown Manhattan was also closed for several days and ready access was limited for over a month. Fears of further terrorist attacks were exacerbated by the anthrax scare on the 18<sup>th</sup> of that same month. As you might recall 22 people were infected and 5 died. Panic ensued across the country concerning biological, chemical and possible nuclear attacks. Low- altitude parachutes were spurred by demand in metropolitan cities. Yet the financial markets have reacted much more negatively to Covid-19 than 9/11.

**However, it appears that the pandemic has started to abate in China; yet the financial markets have ignored this improvement.** What is it that the markets know that we don't? What we do know is that estimates of U.S. growth have been downgraded a number of times in these few short weeks since the emergence of the Covid-19, from a 2020 growth target of 2.5% to now 1.2%. In our opinion, these negative forecasts have already been factored in. As of last week, economists like Goldman Sachs are now calling for a growth forecast to drop further, to 0.4% for 2020, comprised of annualized real GDP growth of 0% in Q1, -5% in Q2, +3% in Q3 and +4% in Q4. While their economist Hatzius has not formally called for a recession, he thinks there is a high probability that the business-cycle at the BEA would classify the new forecast as a recession albeit temporary.

**In the midst of uncertainty in terms of the longevity and severity of the impact from the virus, we continue to recommend staying invested, as Congress finalizes measures to stimulate the economy.** This should define a floor to the economic contraction. Keep in mind that this contraction was not borne out of major financial and economic imbalances, with household savings and corporations in much better shape to absorb this shock. Stocks have already fallen nearly 30% from the peak discounting a typical recession. Oil prices and Treasury yields appear to be forming a floor and volatility in the market is near levels reached in the trough of the Global Financial Crisis of 2008-09. No doubt we were surprised by the speed and magnitude of the market's peak-to-trough decline. In fact, this was the fastest decline from an all-time-high in market history. In our view, the market decline is pricing a 90% probability of a recession. These are unsettling times and we certainly don't want to seem overly optimistic or dismissive.

**However, while we are very concerned, we do not believe that this disturbing turn of events is likely to impact our longer-term approach to the markets.** Ultimately, we do not believe that it will permanently impair the underlying intrinsic values of our holdings. Staying true to many of the great investors like Benjamin Graham, we stay focused on the fact that a stock purchase represents ownership in a real business enterprise that has a value which is often independent of the price at which it trades in the stock market. In other words, we can – and do – own companies that can sustain their business models through a recessionary period. In critical times like today, we stand resolute with our conviction that challenging markets provide attractive buying opportunities. Taking advantage of those opportunities as they become apparent is what a successful long-term investment program is all about.

**Our conclusion is that we are in a bear market that is feeding on the pandemic of fear.** We expect that investor fear will dissipate by the summer as the virus pandemic abates. The downside is likely to be near current levels and this bear market is looking more like the 1987 sell-off than the declines of 2008-2009. We expect that there will be a big rebound in the economy during the fall - and stocks will follow suit. What about achieving the record high in February? It is likely to be achieved next year.

As a final thought, we are reminded of a quote by Seth Klarman, a widely respected investor in the financial industry:

*“To maintain a truly long-term view, investors must be willing to experience significant short-term losses; without the possibility of near-term pain, there can be no long-term gain. The ability to remain an investor (and not become a day-trader or a bystander) confers an almost unprecedented advantage in this environment”.\**

\* Seth Klarman, “The Value of Not Being Sure,” *Value Investor Insight*, February 23, 2009

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