Weekly Recap: COVID-19 Market Edition

For the week ending March 27, 2020

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Commentary

Since the end of February, equity and Treasury volatility spiked to 2008 levels due the rapid spread of COVID-19 and the impending halt to economic growth. Even more alarming is the velocity in which these market moves are taking place. During the infancy of the Great Financial Crisis in 2007, it took 190 trading days for the S&P 500 index to fall into a bear market. Furthermore, it took 63 trading days for the S&P 500 index to fall 19.36% during the Q4 2018 correction. Meanwhile, it only took 15 trading days for the S&P 500 index to fall into a bear market during the current COVID-19 crisis.

Along with previous crisis', correlations between asset classes have increased. Since reaching its all time high on February 19th, the S&P 500 index has fallen over 24% through March 27th, while safe haven Treasuries (7-10 Year Treasury Bond iShares ETF (IEF) have increased 6.45% but have experienced volatility and sell-offs that have corresponded with deep equity sell-offs. Gold, which is the ultimate hedge to economic and market turmoil, has been flat between February 19th and March 27th. Finally, the U.S. dollar (DXY) fell initially, however, the greenback recovered and posted a -0.27% return despite the Fed slashing rates and employing massive monetary stimulus packages. It is hard to pinpoint the reason for these unusual market moves other than investors are selling everything to pay bills, cover margins, or are discounting the flood of debt that is about to take place to cover the huge stimulus packages. Or, investors are truly concerned about the future and dashing to cash.

The economy is sure to feel the effects of the closed business', social distancing, and "shelter in place" strategies as the odds for a U.S. recession in 2020 sits at 88%, according to PredictIt. Jobless claims was the first shoe to drop as claims rose to jaw dropping levels, while the flash PMIs fell sharply. Although the economic data releases painted a dire picture of what lies ahead, markets rallied (S&P 500 index +10.28%) during the week as investors focused on fiscal and monetary policies. Additionally, we are starting to see the impact the outbreak had on the Chinese economy with their industrial production falling to -13.5%, retail sales coming in at -20.5% and fixed investment also falling a -25.5%. It is all but certain that the U.S. and potentially the global economy will fall into a recession, if it hasn't already. We must now focus on the depth and duration of the recession. The answers to those two questions depend on the ongoing COVID-19 outbreak and how soon will we see the peak and subsequent decline in new cases. I do believe the recession will be harsh, considering the large portions of the economy that are shut down and subsequent spike in unemployment.

Turmoil in the corporate credit space, which has ballooned to historic levels during this low interest rate era, has added to investor angst. Credit spreads have reached distressed levels for high yield debt, which will lead to an increase in defaults and bankruptcies, particularly the "zombie corporations", while financial stress indicators such as the TED spread and Libor-OIS spreads have increased. Fallen angles, such as Ford, are set to increase as highly leveraged companies are sure to see revenues fall and liquidity shrink. In addition to the above credit risk, liquidity risk has been a major concern for investors, corporations, and central banks. Spiking yield spreads on commercial paper (+179 bps), BBB investment grade debt (+440 bps), and high yield debt (+1000 bps) added to the liquidity concerns. Furthermore, wide bid/ask spreads for Treasuries and historically wide discount to NAV spreads for bond ETFs were another sign of bond market dislocations. These dislocations prompted the Fed to cut rates to zero while implementing unlimited QE and taking other unprecedented steps to backstop investment grade debt, MBS, Municipals and bond ETFs in an effort to stabilize the bond market, inject liquidity, and make sure debt markets continued to function. After initially spiking following the Fed's decision to slash Fed Fund rates, yields on 10-year Treasuries have decreased, which is more in line with expectations following such a move. However, the unprecedented monetary stimulus helped stabilize markets and contributed to the rally in markets. However, the Fed's actions to stabilize the credit markets along with the fiscal stimulus package will help ease concerns that this crisis will become a credit crisis rather then a demand crisis. There will be fallen angels and defaults, but the willingness of policy makers to backstop markets and corporations will provide rating agencies with enough confidence to reduce the number of downgrades from investment grade to junk. However, if credit spreads continue to show more distress, and the unwinding of the credit cycle picks up speed the crisis will become a credit crisis.

This week's rebound was more of a head fake than the beginning of a recovery, as I do not believe we have hit capitulation yet. Uncertainty remains high as we are still early in gathering economic data, sentiment has not fallen enough, equity positions held at asset and institutional managers have more room to fall, and sector performance shows the rally was a defensive one. Moving forward, following the Fed's footsteps is a good place to start as you can take comfort in knowing that the Fed will provide liquidity to assets that were illiquid, such as investment grade bonds. Indicators to watch include credit spreads, which currently are no where near their 2008 levels, and may continue to climb higher until reaching an inflection point. Finally, follow the relationship between the dollar and U.S. equities, as equity bottoms have coincided with the peak of the dollar in past recessions. It is entirely too early to make wagers on when the outbreak will subside, and economic growth will recover. With that being said, it will be imperative for investors to focus on their individual goals and objectives during this uncertain time and looming economic recession. Continue to focus on high quality companies who hold excess cash and provide a steady dividend, while also focusing on high quality debt. Finally, continue to look for investments that reduce portfolio correlations such as real assets and short-term Treasuries.

Global Asset Class Performance

Major Equity Asset Class Performance

Index	1 Week	3-Mos	YTD	1 Year	3 Year	Flows (mil)
S&P 500	10.28%	-5.50%	-8.27%	8.19%	9.87%	($11,067)
Russell 3000	10.70%	-5.64%	-8.29%	6.90%	9.28%	($15,588)
Russell 1000	10.64%	-5.42%	-8.07%	7.82%	9.73%	($8,583)
Russell MidCap	13.54%	-7.34%	-9.42%	2.34%	6.57%	($1,474)
Russell 2000	11.68%	-8.80%	-11.36%	-4.92%	3.52%	($305)
MSCI EAFE	11.23%	-8.01%	-10.92%	-0.05%	4.44%	($1,967)
MSCI EM	4.95%	-2.88%	-9.68%	-1.51%	5.28%	($1,921)
MSCI World	10.71%	-6.18%	-8.94%	5.23%	7.84%	($24,241)

Equity Style Performance

1 Mos	Value	Blend	Growth
Large	-9.68%	-8.17%	-6.81%
Mid	-9.90%	-8.69%	-6.90%
Small	-9.72%	-8.42%	-7.22%

YTD	Value	Blend	Growth
Large	-11.63%	-8.07%	-4.73%
Mid	-11.66%	-9.42%	-6.02%
Small	-14.59%	-11.36%	-8.24%

Equity Factor Performance

Factor Index	3 Mos	YTD	1 YR Risk-Adj %
MSCI USA Small Cap	-8.81%	-11.14%	-2.83%
MSCI USA Value	-9.48%	-11.95%	0.34%
MSCI USA Minimum Volatility	-4.18%	-5.96%	11.98%
MSCI USA Momentum	-2.20%	-3.93%	13.62%
MSCI USA Quality	-3.53%	-6.94%	14.14%
MSCI USA Dividend Tilt	-7.67%	-10.13%	4.39%

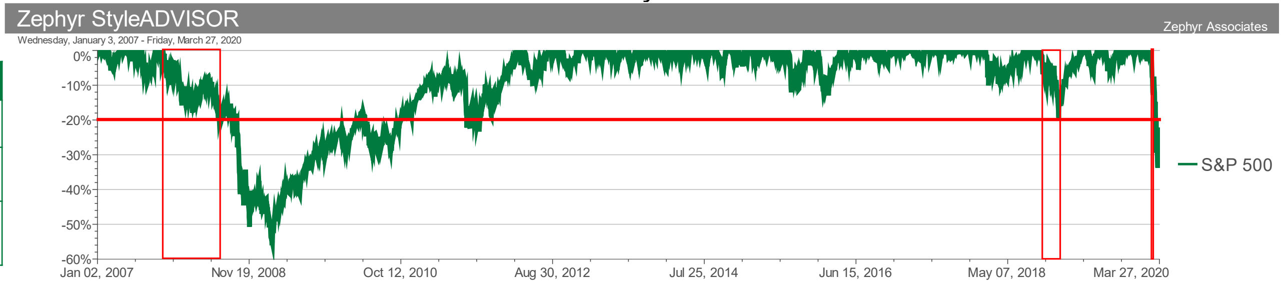
Major Fixed Income Asset Class Performance

Index	1 Week	3-Mos	YTD	1 Year	3 Year	Yield
Bloomberg Barclays US Aggregate	2.66%	3.69%	3.76%	11.68%	5.01%	1.62
Bloomberg Barclays US High Yield	5.06%	0.59%	-1.38%	6.10%	4.86%	9.90
Bloomberg Barclays Municipals 10 Yr	8.26%	3.54%	3.14%	9.29%	5.53%	1.76

Rates

	3/27/20	3/20/20	12/31/19	12/31/19	3/27/19	3/27/17
2-yr U.S. Treasuries	0.25	0.37	1.58	1.58	2.22	1.27
10-yr U.S. Treasuries	0.72	0.92	1.92	1.92	2.39	2.38
30-yr U.S. Treasuries	1.29	1.55	2.39	2.39	2.83	2.98
10-yr German	-0.44	-0.28	-0.19	-0.19	-0.07	0.37
10-yr Japan	0.01	0.09	-0.03	-0.03	-0.07	0.05
10-yr U.K.	0.28	0.50	0.74	0.74	0.96	1.10

Chart of the Week: Velocity of S&P 500 Drawdowns



Wednesday, January 3, 2007 - Friday, March 27, 2020: Summary Statistics

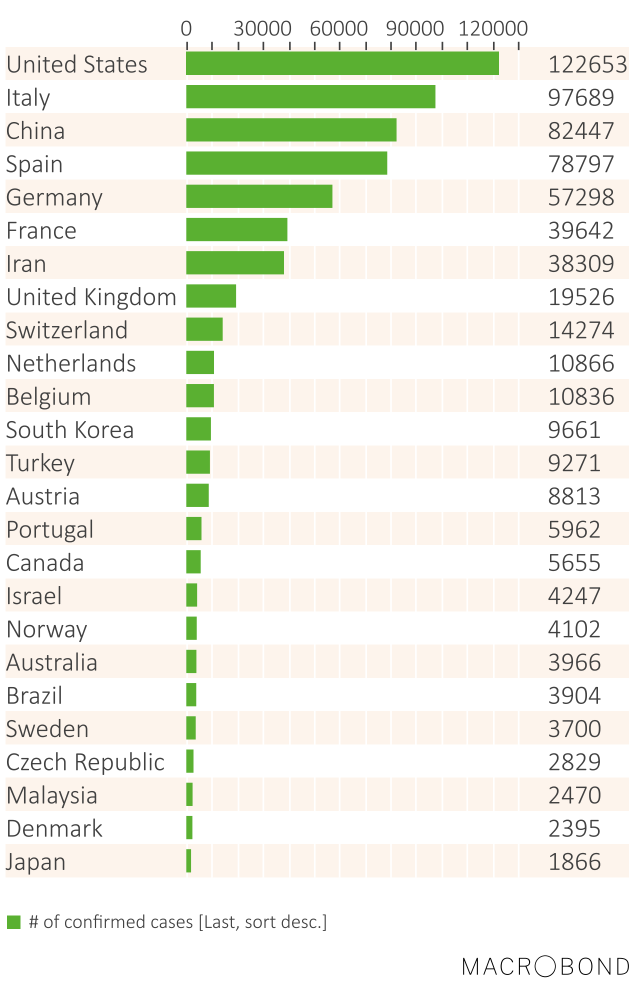
	Max Drawdown	Max Drawdown Begin Date	Max Drawdown End Date	Max Drawdown Length	Max Drawdown Recovery Date	Pain Index	Pain Ratio	Gain to Loss Ratio	High Water Mark Date	To High Water Mark
S&P 500	-55.25%	Oct 10, 2007	Mar 9, 2009	355	Apr 2, 2012	8.70%	0.65	0.89	Feb 19, 2020	32.95%

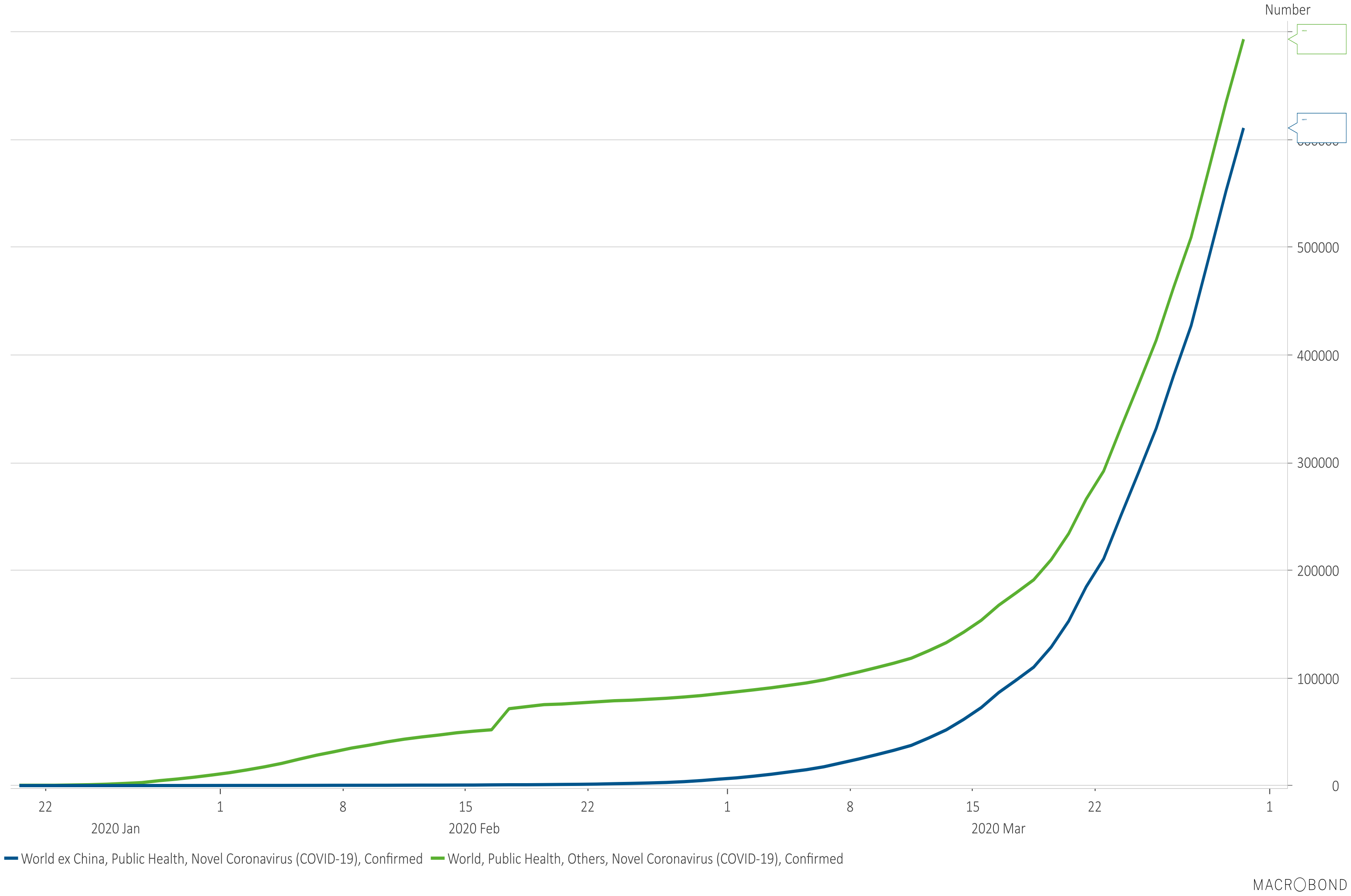
Thursday, January 2, 2020 - Friday, March 27, 2020: Summary Statistics

	Max Drawdown	Max Drawdown Begin Date	Max Drawdown End Date	Max Drawdown Length	Max Drawdown Recovery Date	Pain Index	Pain Ratio	Gain to Loss Ratio	High Water Mark Date	To High Water Mark
S&P 500	-33.79%	Feb 20, 2020	Mar 23, 2020	23	N/A	8.22%	-2.62	0.75	Feb 19, 2020	32.95%

Sources: Zephyr StyleADVISOR, Macrobond, PSN Enterprise, Bloomberg. 1 week data as of 3/27/20, unless otherwise stated, time periods over 1 week as of 2/29/20. Equity Style Performance represented by: Large Value – Russell 1000 Value, Large Blend – Russell 1000, Large Growth – Russell 1000 Growth, Mid Value – Russell MidCap Value, Mid Blend – Russell MidCap, Mid Growth – Russell MidCap Growth, Small Value – Russell 2000 Value, Small Blend – Russell 2000, Small Growth – Russell 2000 Growth. Fund flow data (EPFR Global) 3/19/20 – 3/25/20, S&P 500 (Large Cap Blend flows), Russell 3000 (all U.S. equity flows), Russell 1000 (all Large Cap flows), Russell Mid Cap (all Mid Cap flows), Russell 2000 (all Small Cap flows), MSCI EAFE (Western Europe DM, Asia Pacific DM flows) MSCI EM (All Emerging Market flows), MSCI World (All Developed Markets flows)

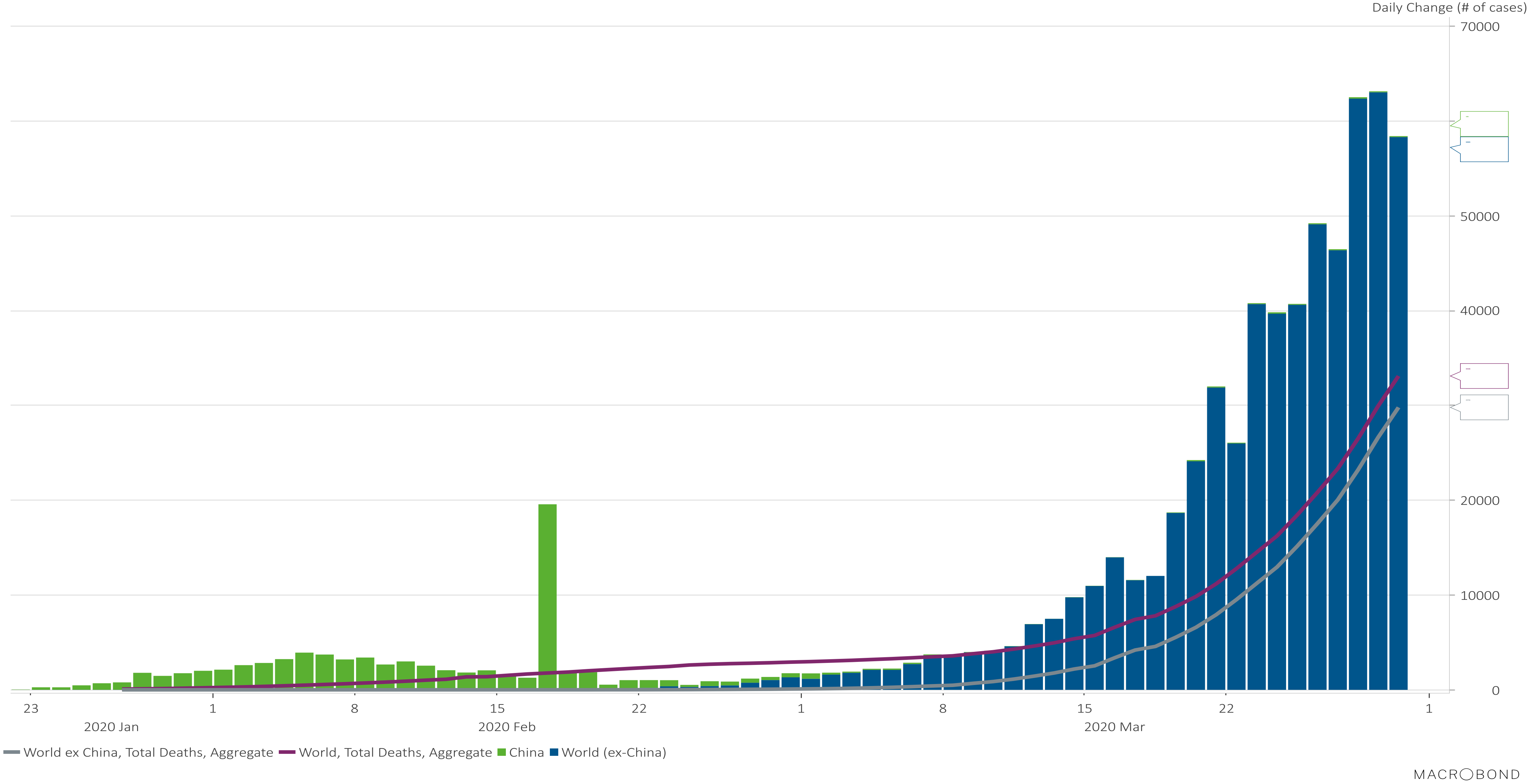
COVID-19 Dashboard: Look for Market Volatility & Economic Weakness To continue Until the COVID-19 Outbreak Peaks





Source: Macrobond, World Health Organization

COVID-19 Dashboard: New Cases Per Day and Total Fatalities Continue to Grow



Source: Macrobond, World Health Organization

Markets: Velocity of Equity Drawdown is Greater Than '08 and '18 Sell-Offs

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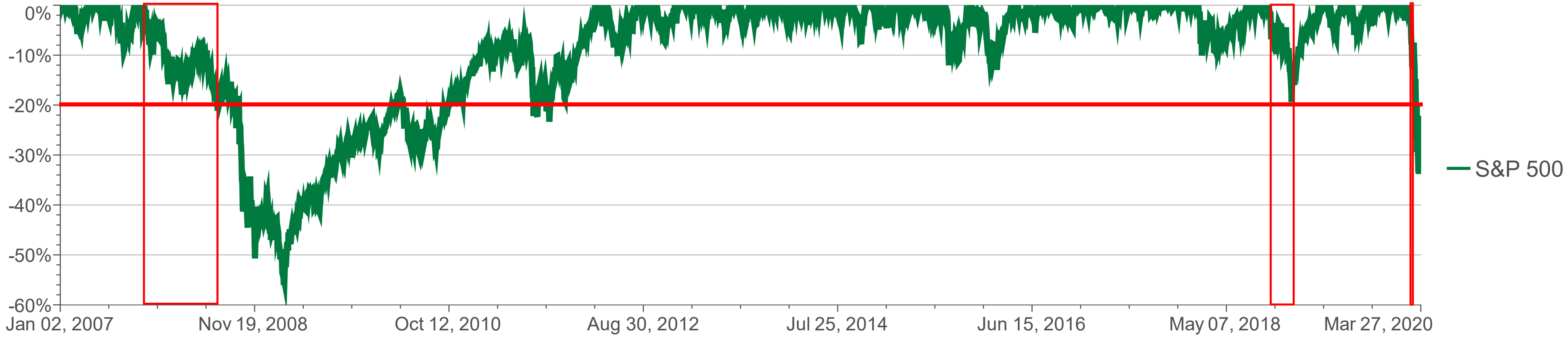

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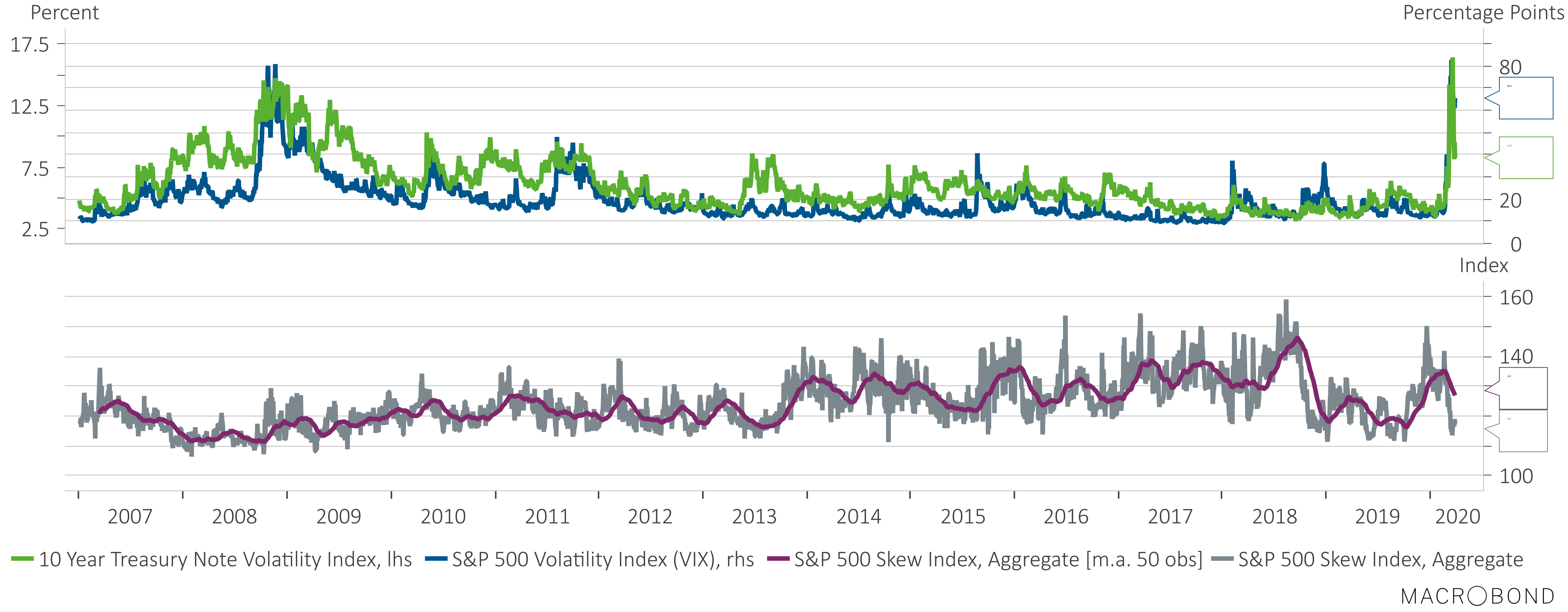
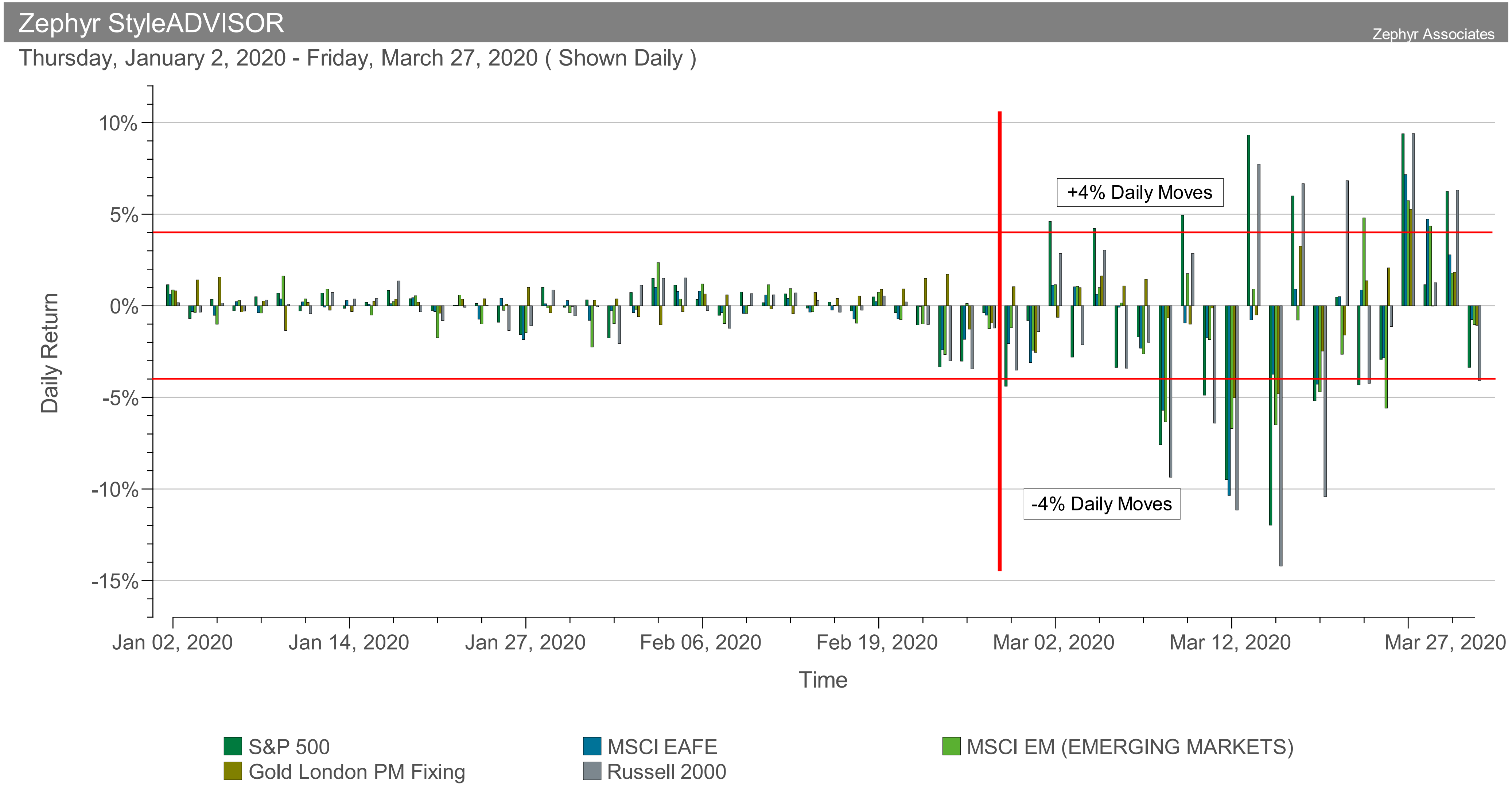
Markets: U.S. CBOE Volatility Indexes Retreat After Eclipsing '08 Highs, While Skew Index (Black Swan Index) Falls Below 50-Day Moving Average Following Stimulus Packages

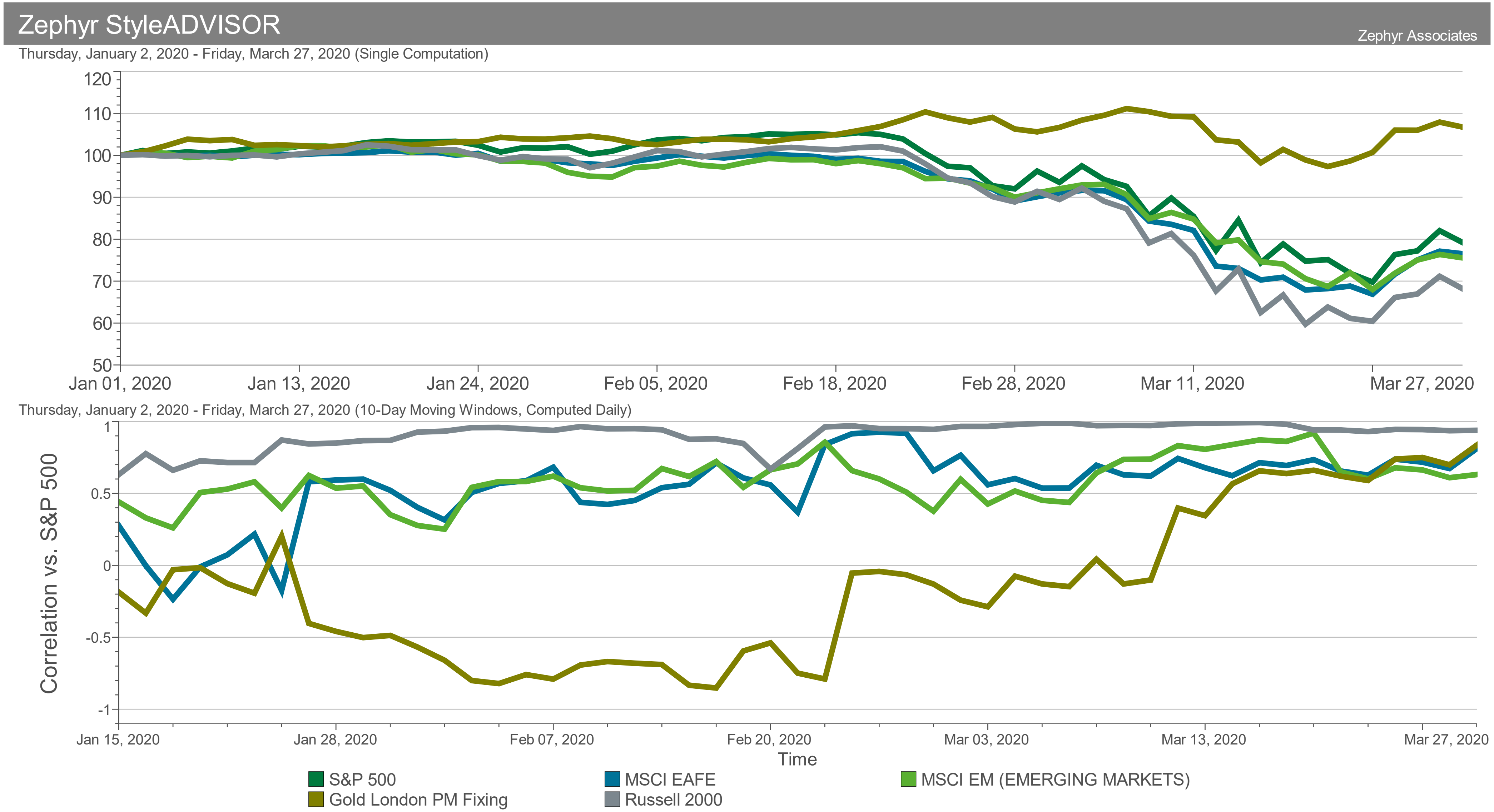


Source: Macrobond, CBOE

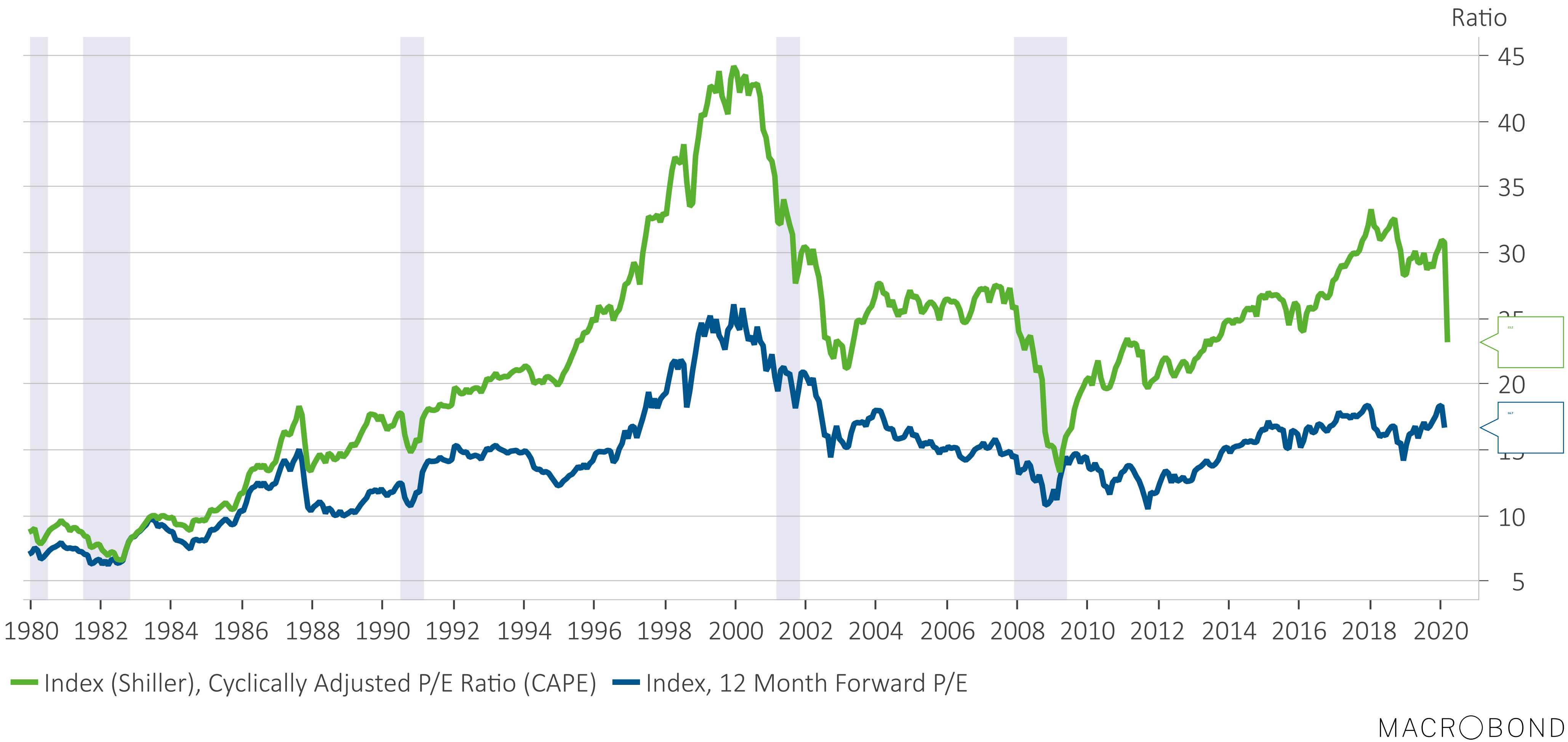
Markets: Daily Swings in S&P 500 Returns Spike to Historic Levels As COVID-19 Spreads and National Economies Shut Down



Markets: Correlations Increase During Crisis', Making it Difficult to Increase Portfolio Diversification During Times of Turmoil

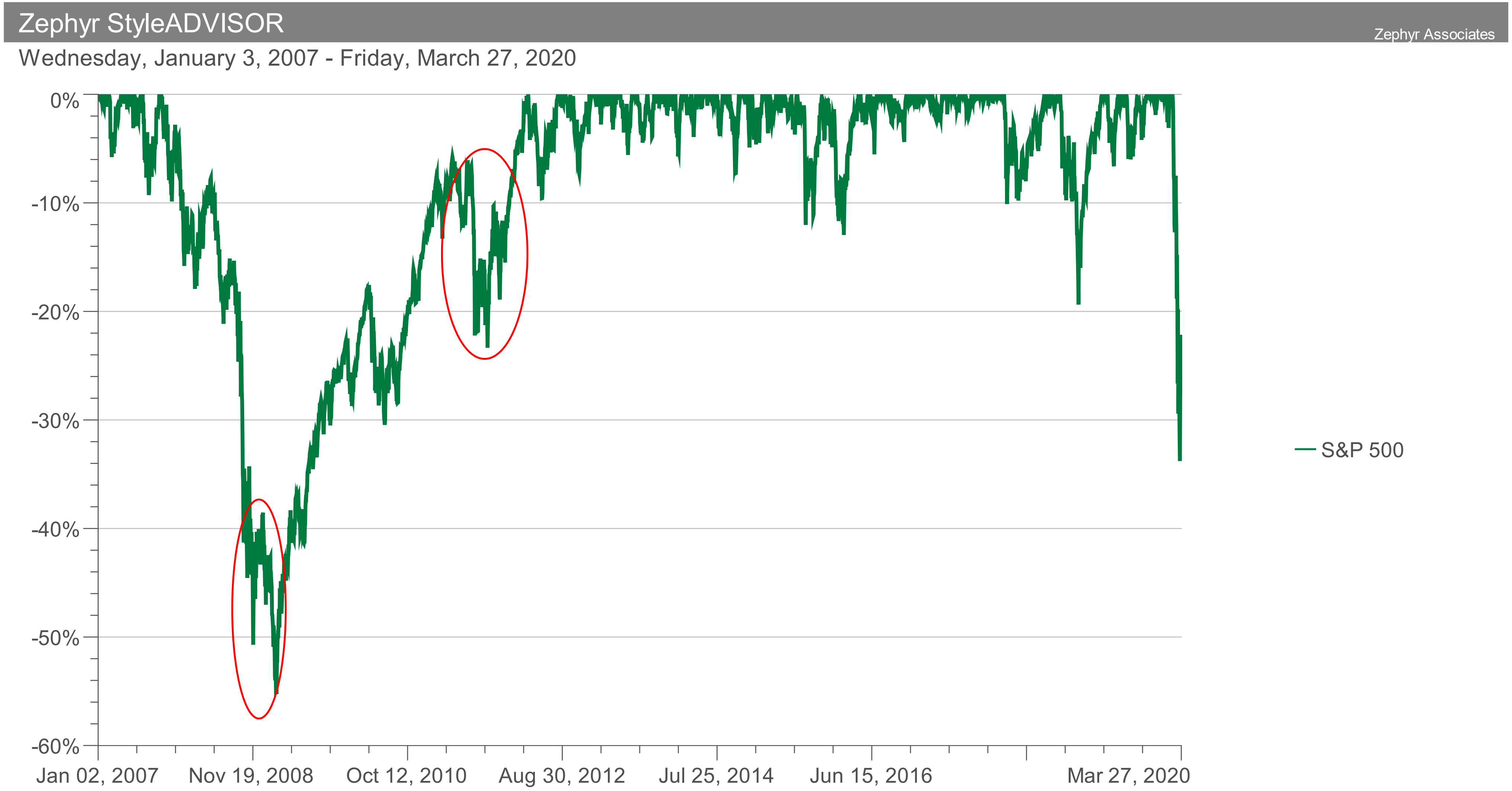


Markets: Despite Falling, S&P 500 P/E Ratio(s) Still Not at '08 Levels



Source: Macrobond, S&P/Robert Shiller, S&P Dow Jones Indices

Markets: Head Fakes, Which This Week's Rally Looks Like, Are Common During Bear Markets



Markets: Equities Enter Bear Markets, While Pain Ratios Fall Below Long-Term Averages

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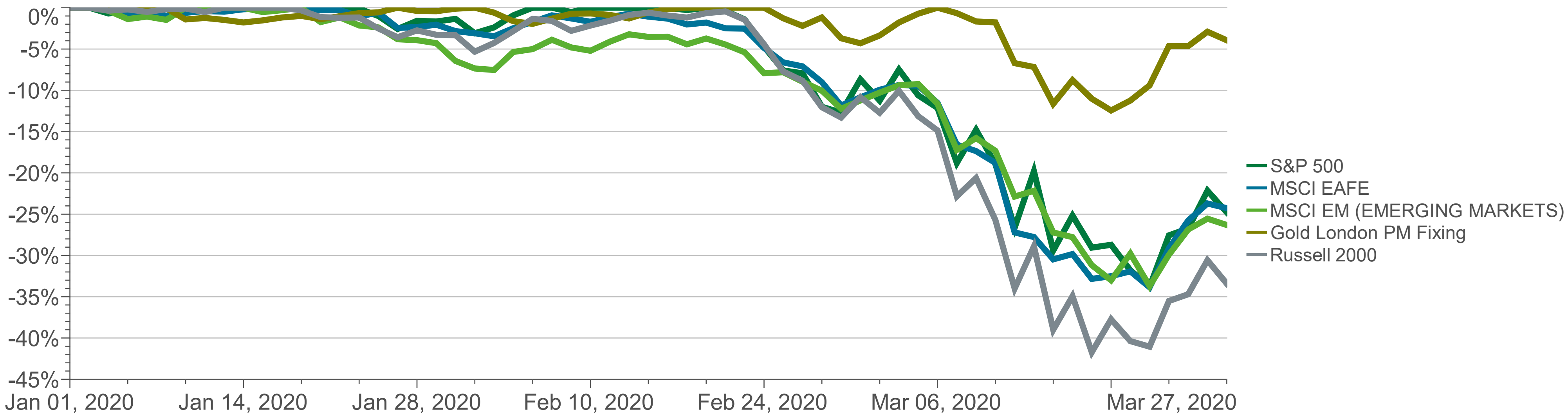

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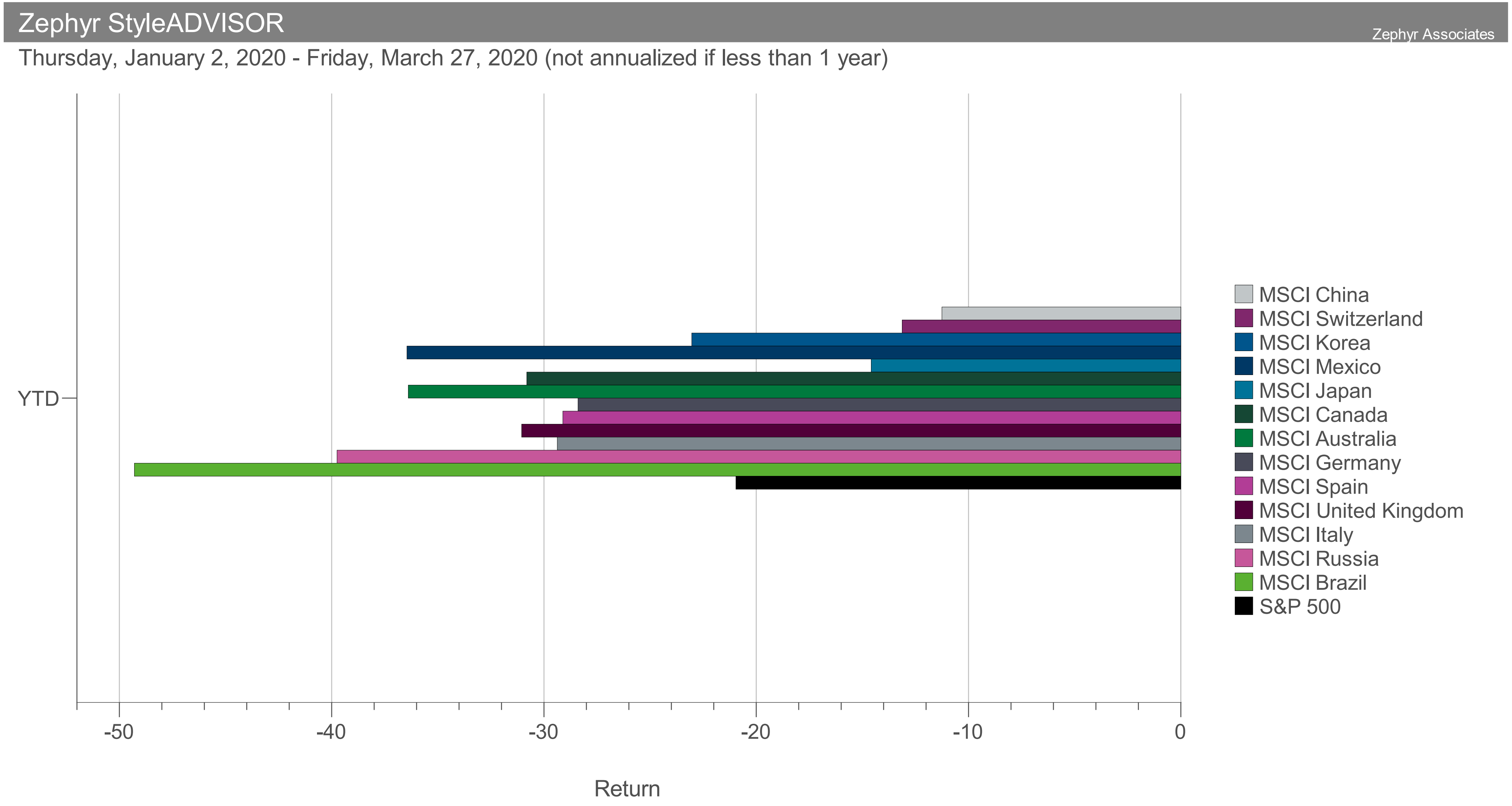
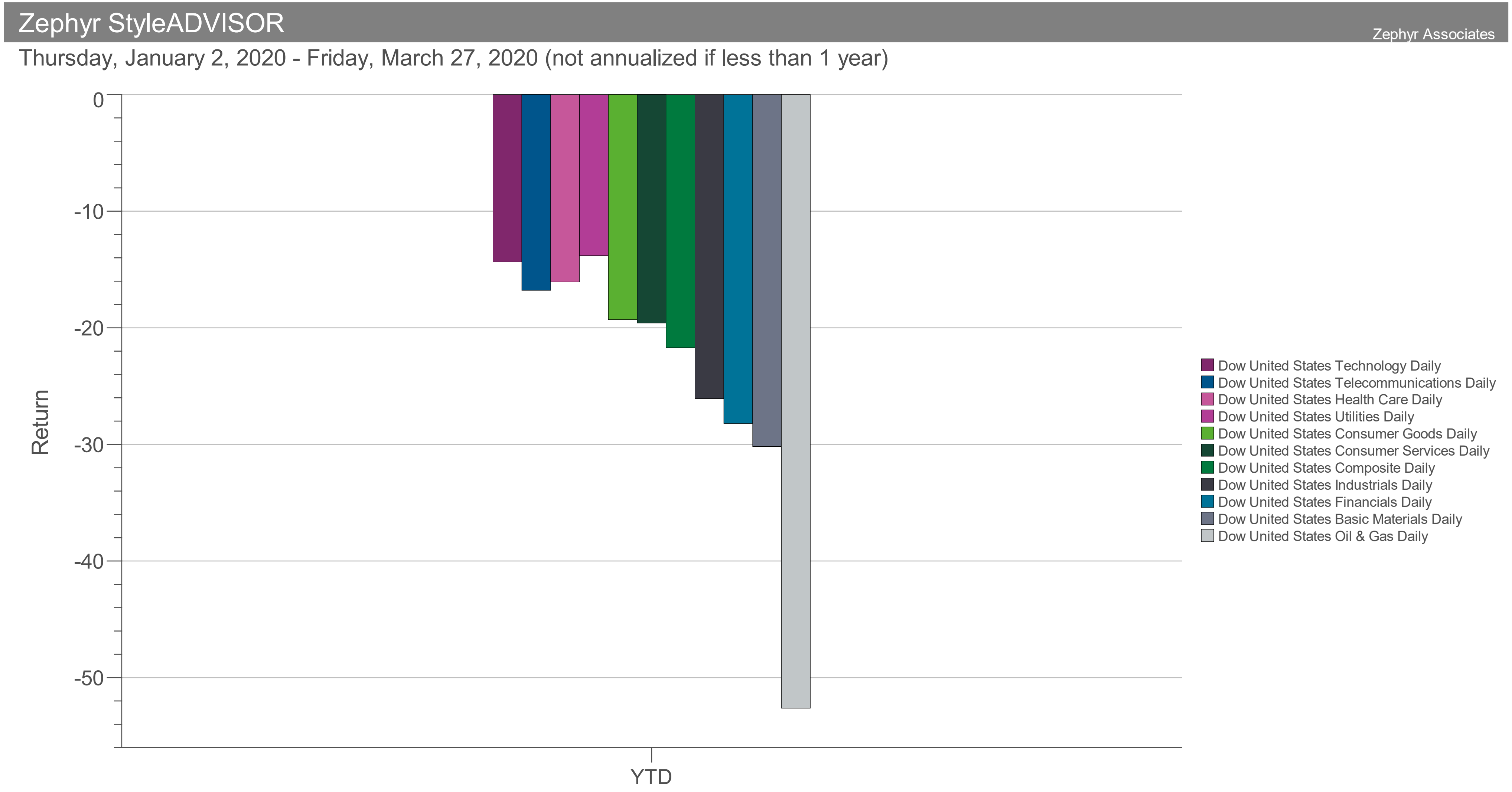
S&P 500	-33.79%	Feb 20, 2020	Mar 23, 2020	23	N/A	8.22%	-2.59	Feb 19, 2020	32.95%
MSCI EAFE	-33.86%	Jan 21, 2020	Mar 23, 2020	44	N/A	8.95%	-2.69	Jan 17, 2020	32.07%
MSCI EM (EMERGING MARKETS)	-33.71%	Jan 21, 2020	Mar 23, 2020	44	N/A	9.80%	-2.55	Jan 17, 2020	35.70%
Gold London PM Fixing	-12.44%	Mar 9, 2020	Mar 19, 2020	9	N/A	2.36%	2.62	Mar 6, 2020	4.10%
Russell 2000	-41.72%	Jan 17, 2020	Mar 18, 2020	42	N/A	10.97%	-2.95	Jan 16, 2020	50.18%
S&P 500	-33.79%	Feb 20, 2020	Mar 23, 2020	23	N/A	8.22%	-2.59	Feb 19, 2020	32.95%

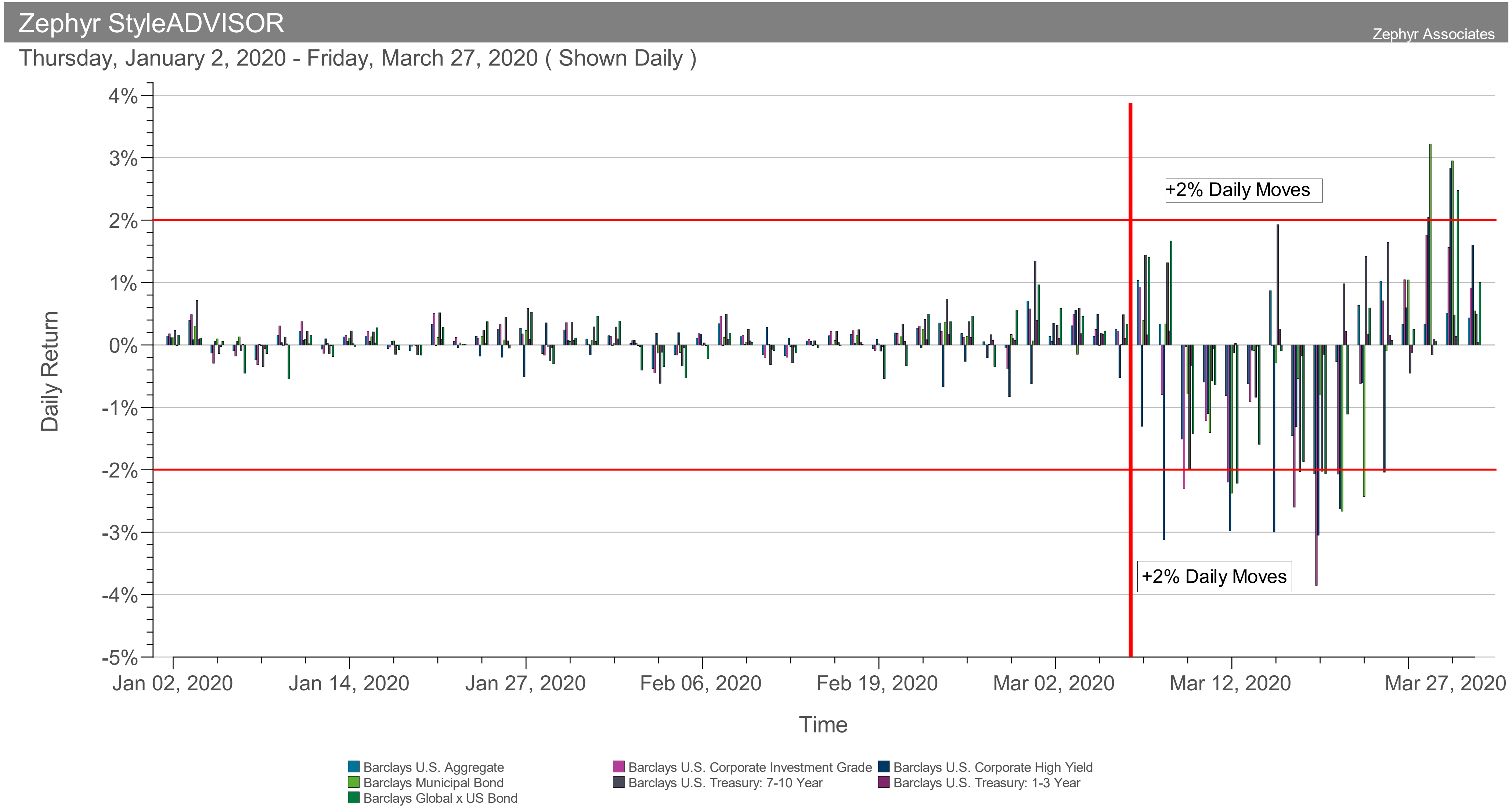
Markets: Despite Having Less Confirmed COVID-19 Cases, Brazilian Equities Have Underperform



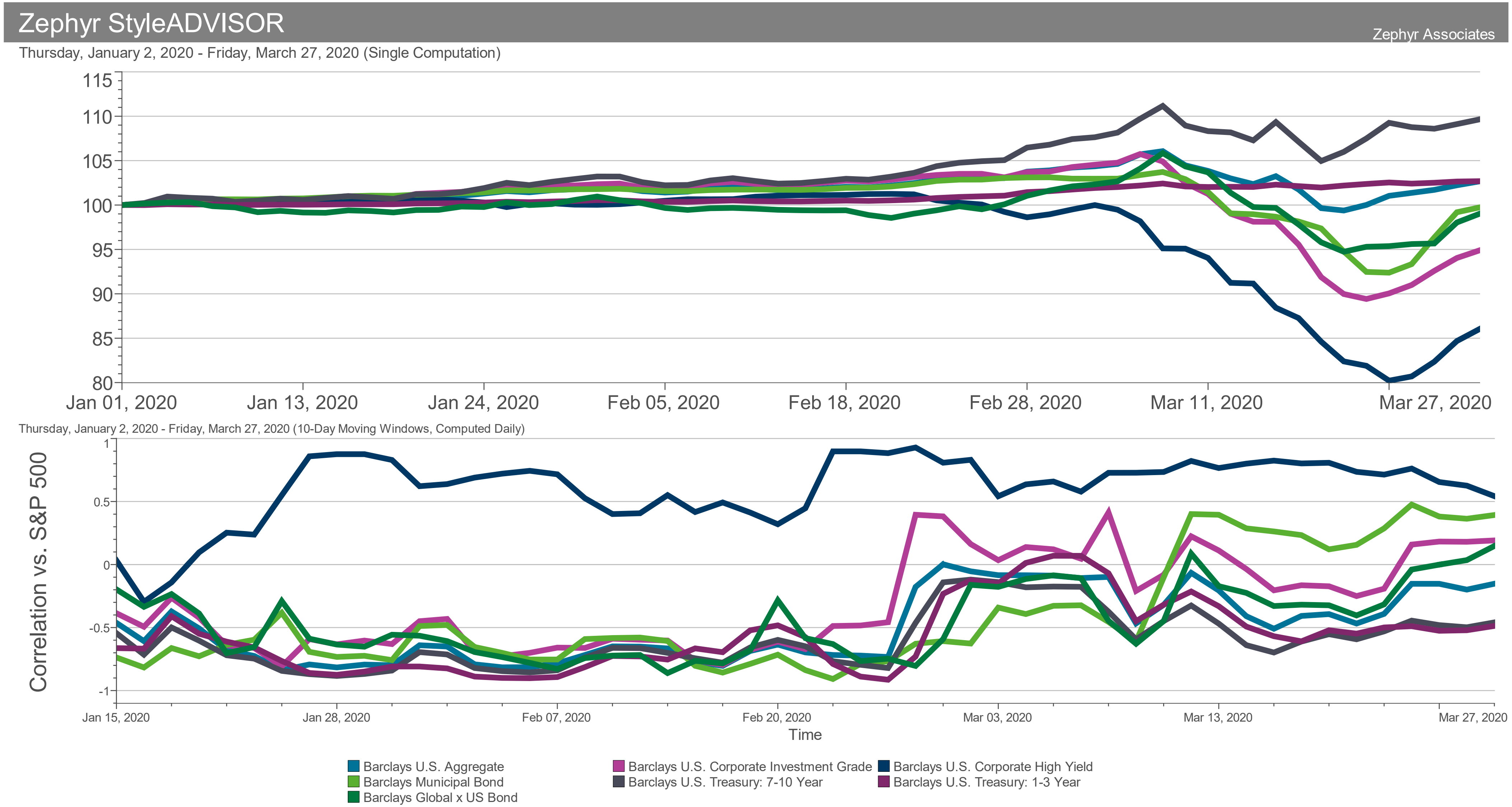
Markets: Telecommunications, Technology, Utilities, and Health Care Sectors Faring Better Than Others



Markets: Fixed Income Experiences Unusually High Daily Swings as Credit Risk Rises and Fed Becomes Buyer of Last Resort



Markets: Correlations Increase During Times of Crisis, Making it Difficult to Increase Portfolio Diversification During Times of Turmoil



Markets: Fixed Income Sectors Reach Correction Territory While HY Bonds Enter a Bear Market

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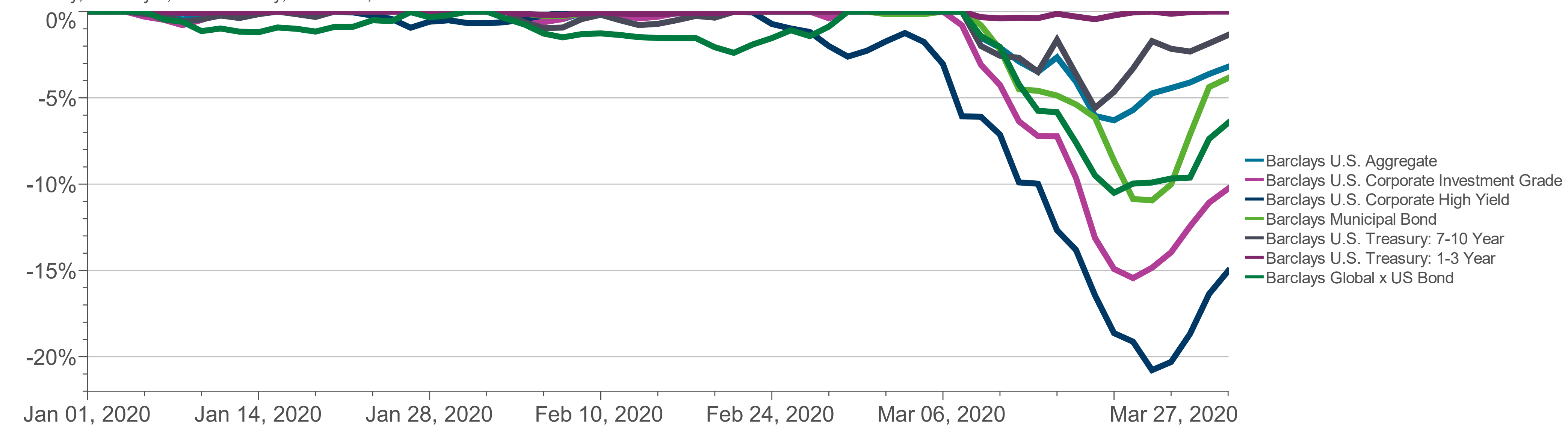
Thursday, January 2, 2020 - Friday, March 27, 2020



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	Max Drawdown	Max Drawdown Begin Date	Max Drawdown End Date	Max Drawdown Length	Max Drawdown Recovery Date	Pain Index	Pain Ratio	High Water Mark Date	To High Water Mark
Barclays U.S. Aggregate	-6.30%	Mar 10, 2020	Mar 19, 2020	8	N/A	0.98%	2.12	Mar 9, 2020	3.31%
Barclays U.S. Corporate Investment Grade	-15.44%	Mar 9, 2020	Mar 20, 2020	10	N/A	2.51%	-2.27	Mar 6, 2020	11.44%
Barclays U.S. Corporate High Yield	-20.78%	Feb 21, 2020	Mar 23, 2020	22	N/A	3.90%	-3.73	Feb 20, 2020	17.69%
Barclays Municipal Bond	-10.94%	Mar 10, 2020	Mar 23, 2020	10	N/A	1.43%	-0.60	Mar 9, 2020	4.01%
Barclays U.S. Treasury: 7-10 Year	-5.58%	Mar 10, 2020	Mar 18, 2020	7	N/A	0.80%	11.33	Mar 9, 2020	1.38%
Barclays U.S. Treasury: 1-3 Year	-0.44%	Mar 10, 2020	Mar 18, 2020	7	Mar 23, 2020	0.08%	27.92	Mar 27, 2020	0.00%
Barclays Global x US Bond	-10.50%	Mar 10, 2020	Mar 19, 2020	8	N/A	2.28%	-0.69	Mar 9, 2020	6.90%
S&P 500	-33.79%	Feb 20, 2020	Mar 23, 2020	23	N/A	8.22%	-2.62	Feb 19, 2020	32.95%

Markets: Performance Divergence Between Blended Portfolios Increase as Volatility Spiked In Late February

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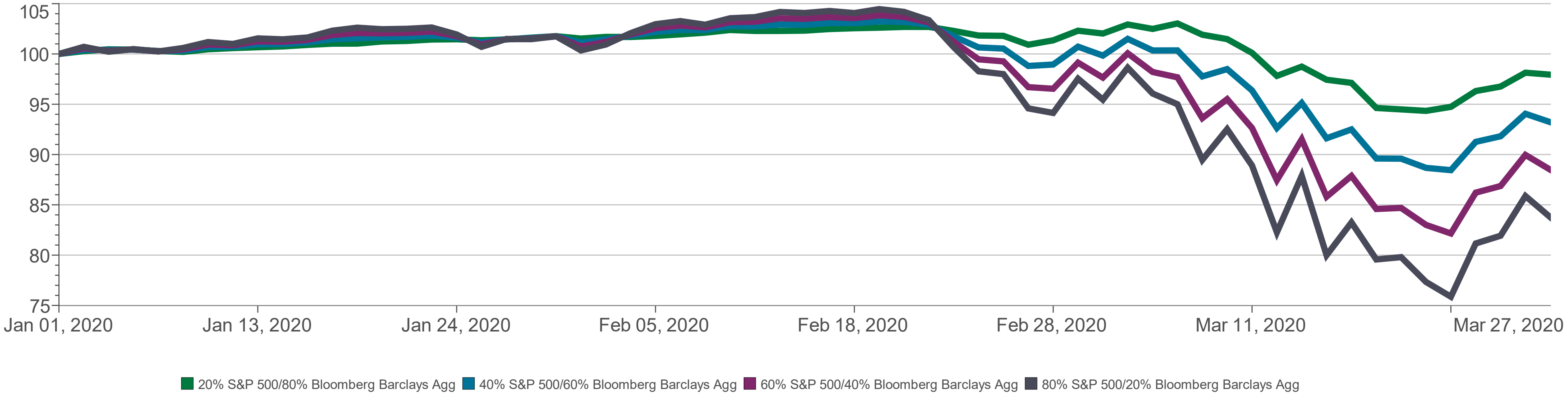
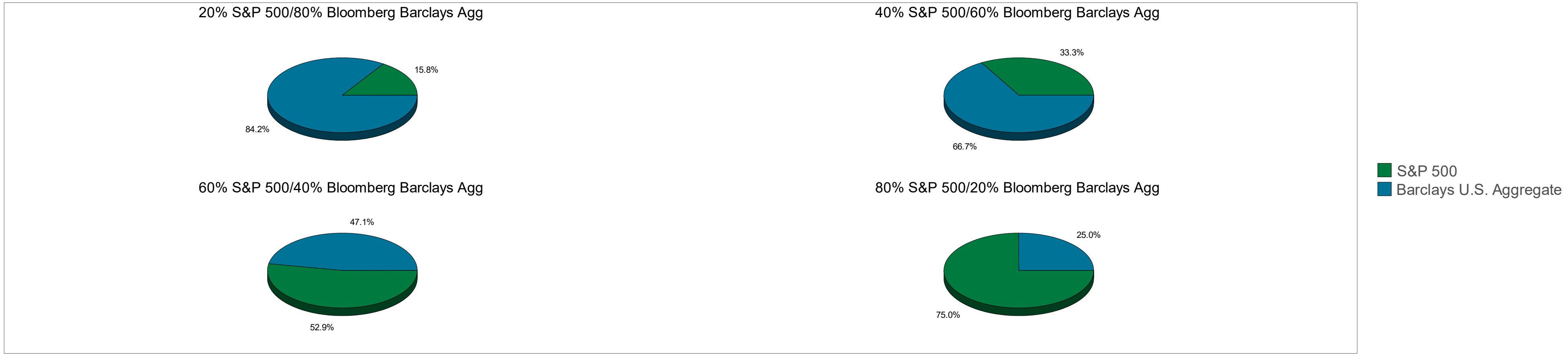
Thursday, January 2, 2020 - Friday, March 27, 2020 (Single Computation)

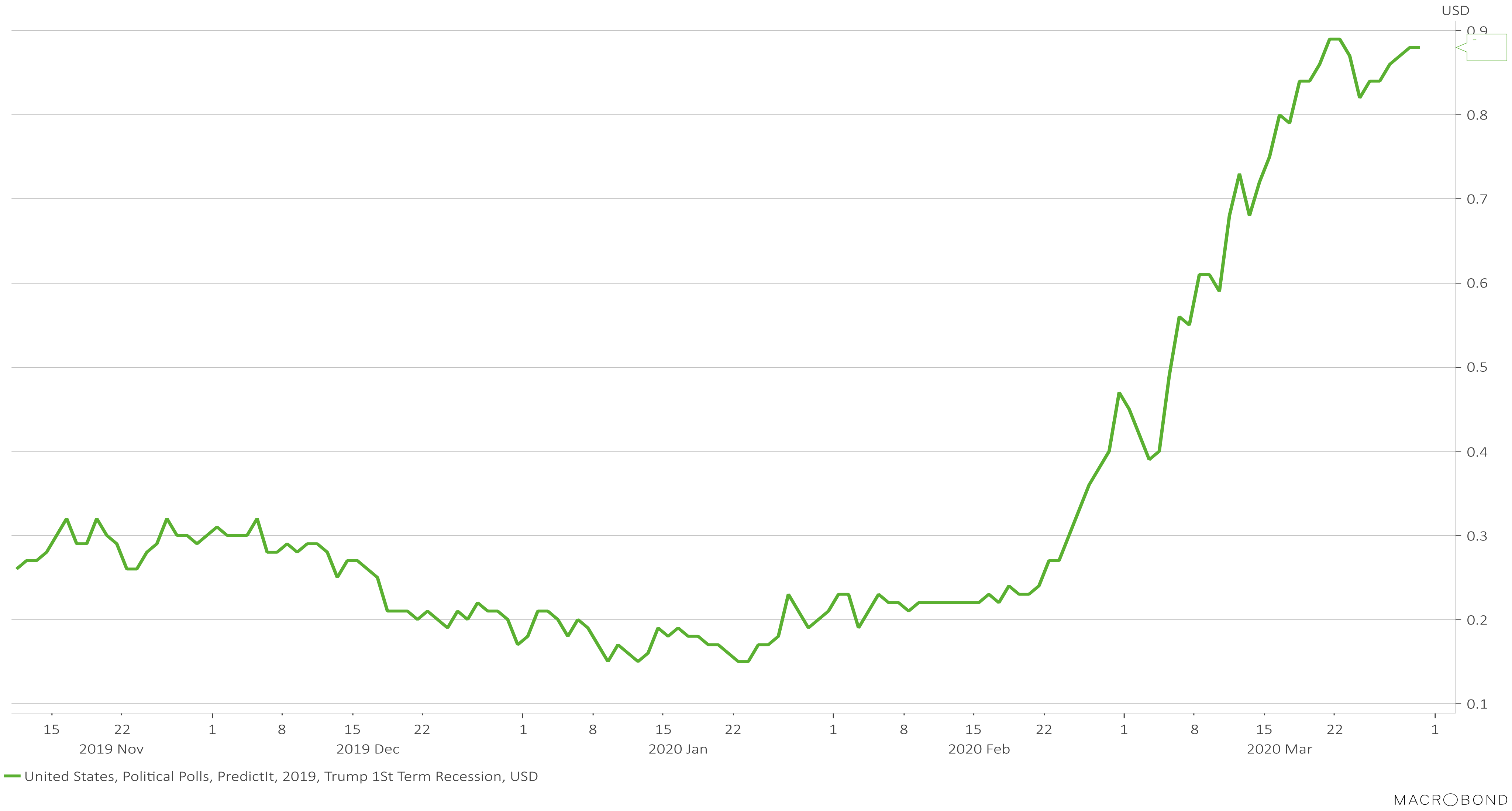


Blend Weights

As of March 13, 2020

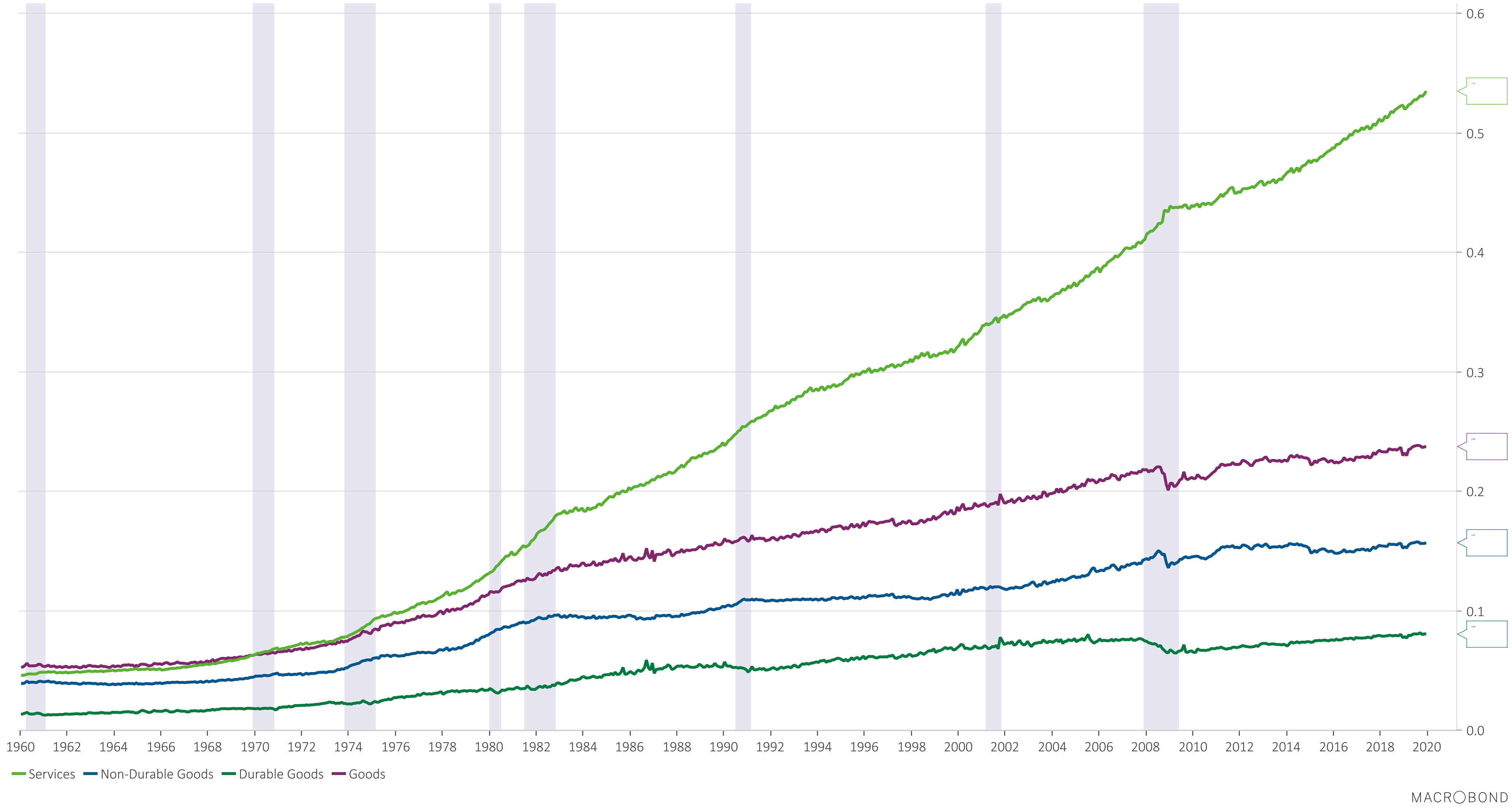


Economy: PredictIt – With a 2020 Recession Nearly Certain, The Duration of The Recession is The Primary Concern



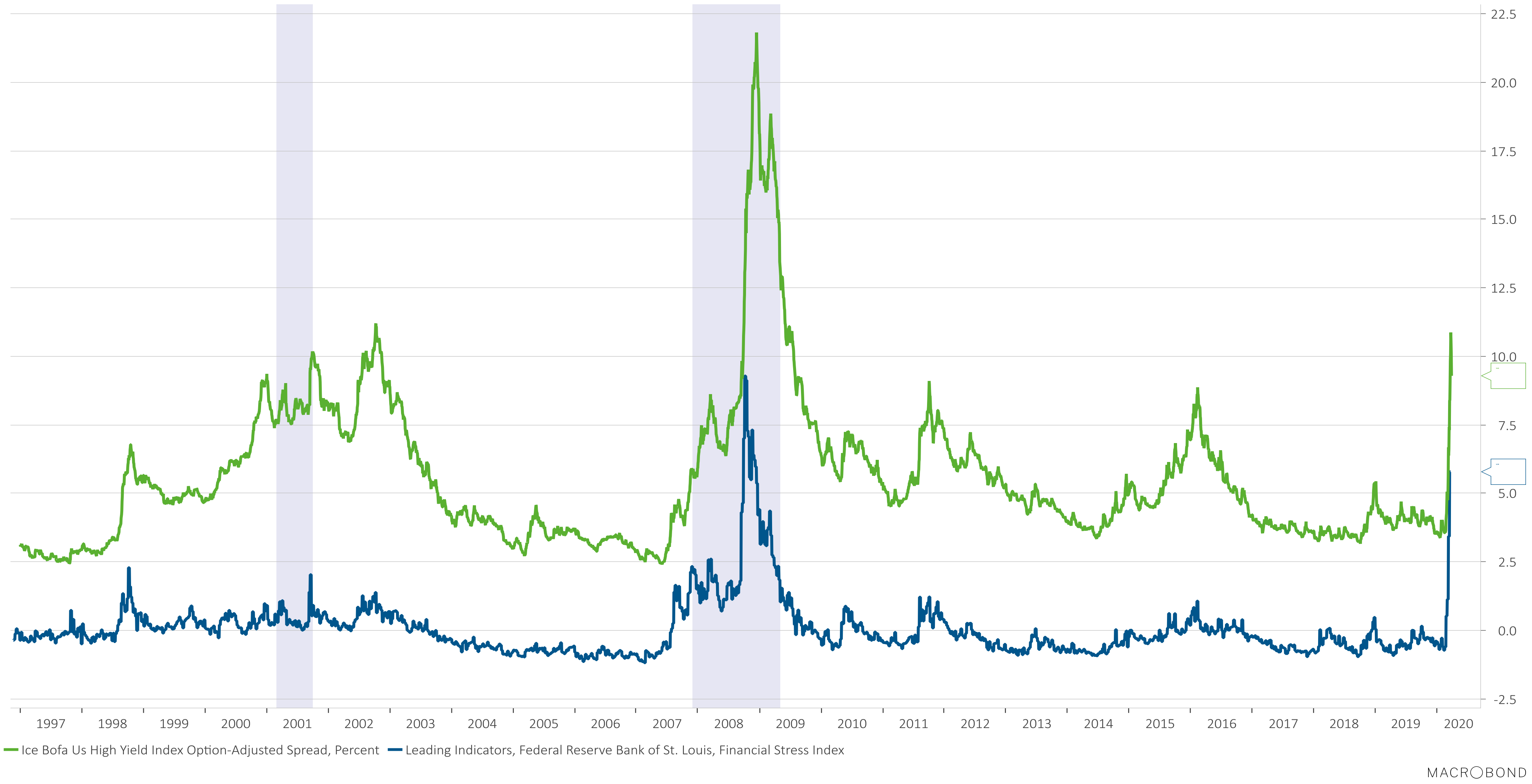
Source: Macrobond, PredictIt

Economy: Services Consumption as % of U.S. GDP Increases During Recessions, Will This Time be Different?



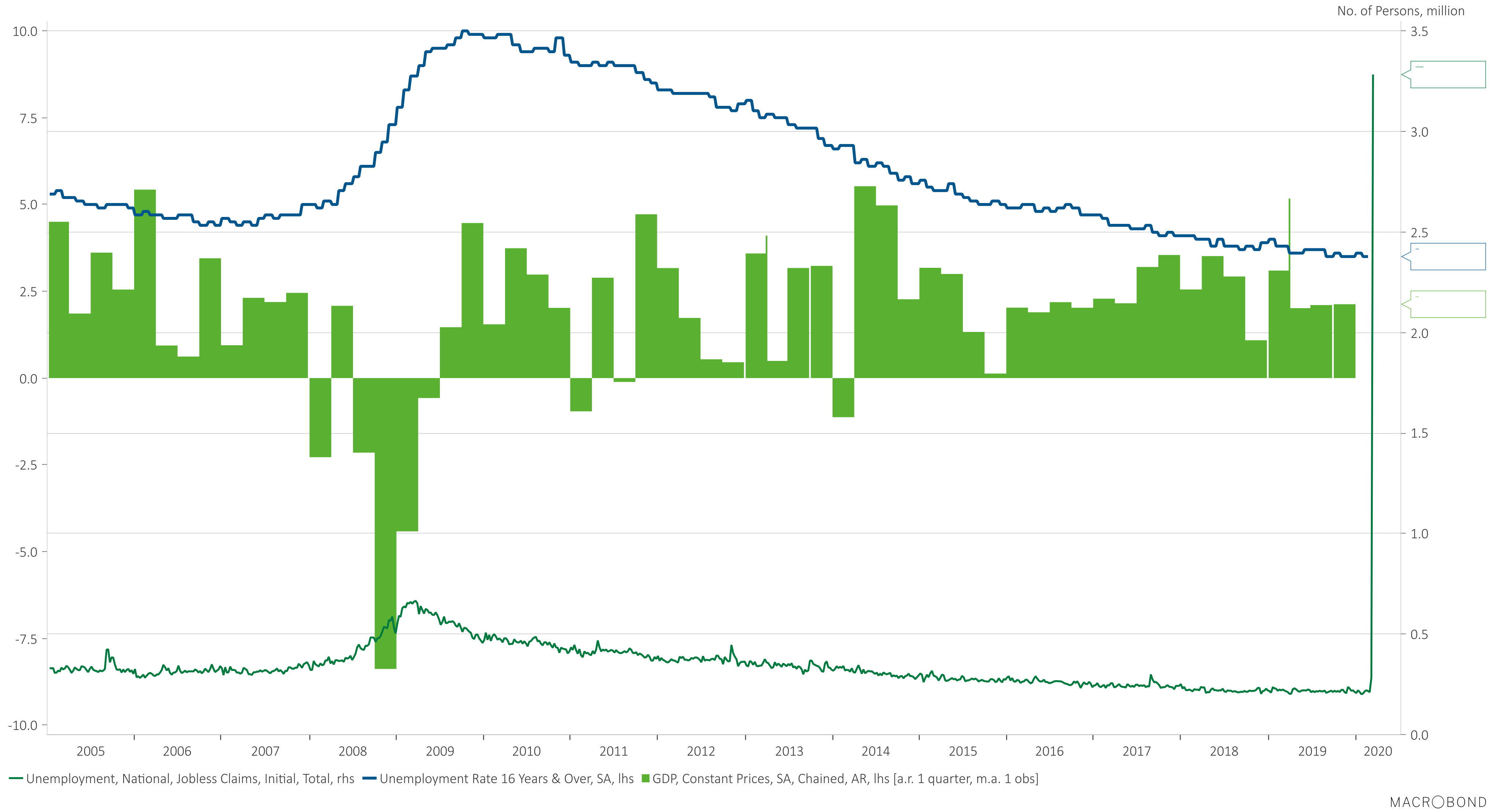
Source: Macrobond, BEA

Economy: Despite Tightening Financial Conditions, Financial Stress Indicators are Far From ‘08 Levels.



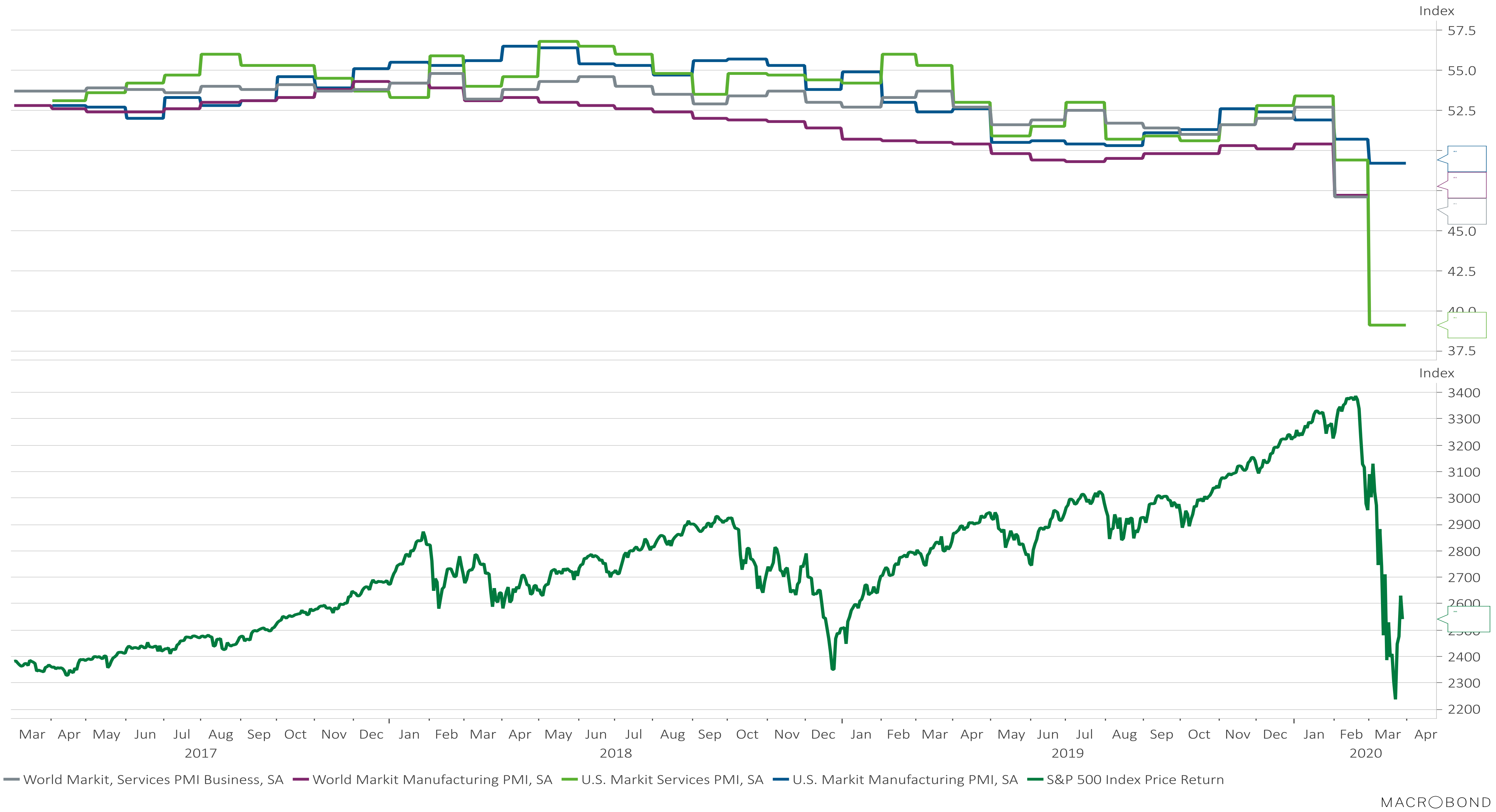
Source: Macrobond, Federal Reserve Bank of St. Louis, ALFRED

Economy: COVID-19 Begins to Take Its Toll On The Economy as Unemployment Claims Spike to Historic Levels



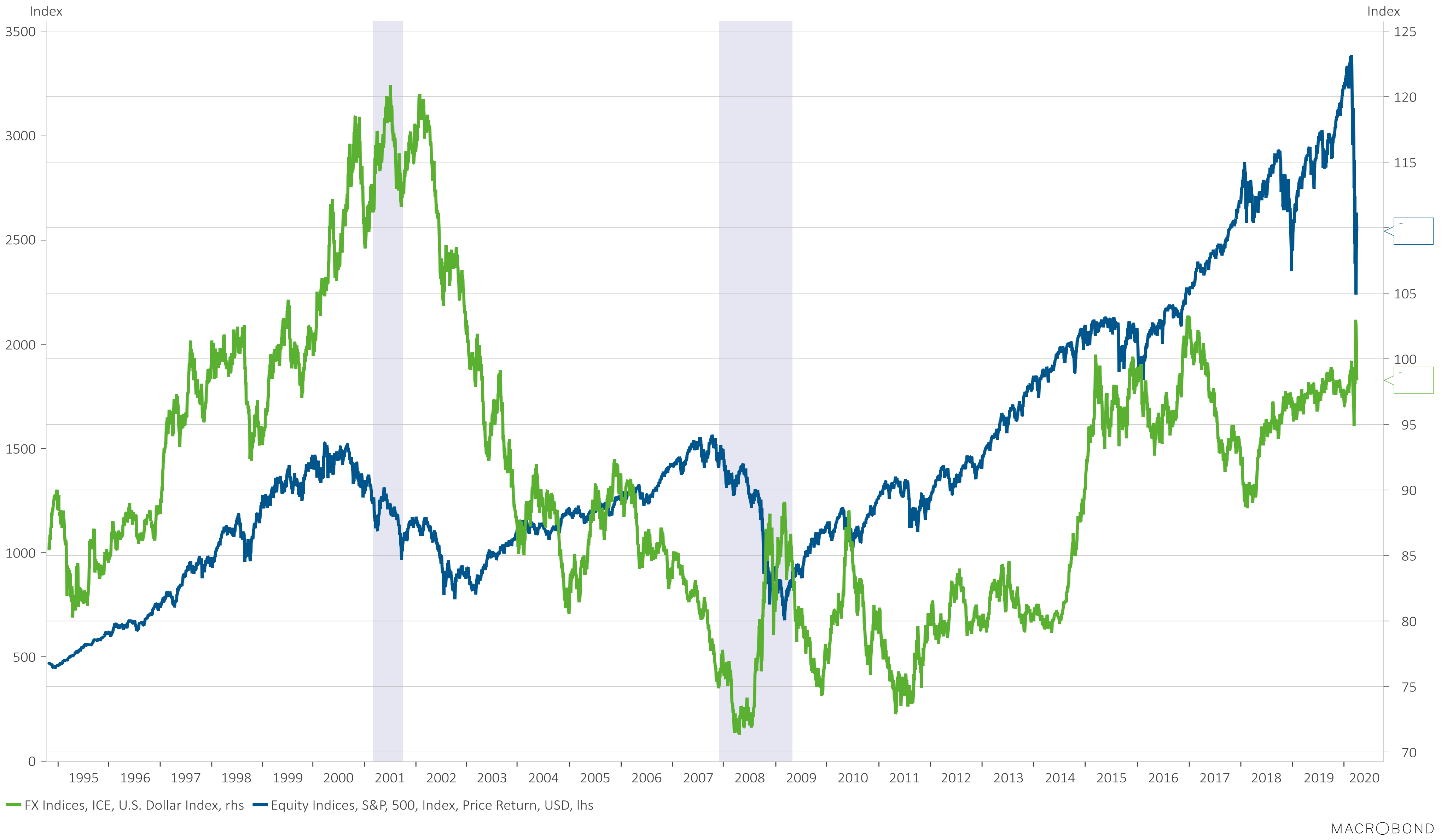
Source: Macrobond, U.S. Department of Labor, BLS, BEA

Economy: Services PMI – The Heart of The Economic Expansion Falls to Historic Levels (39.1)



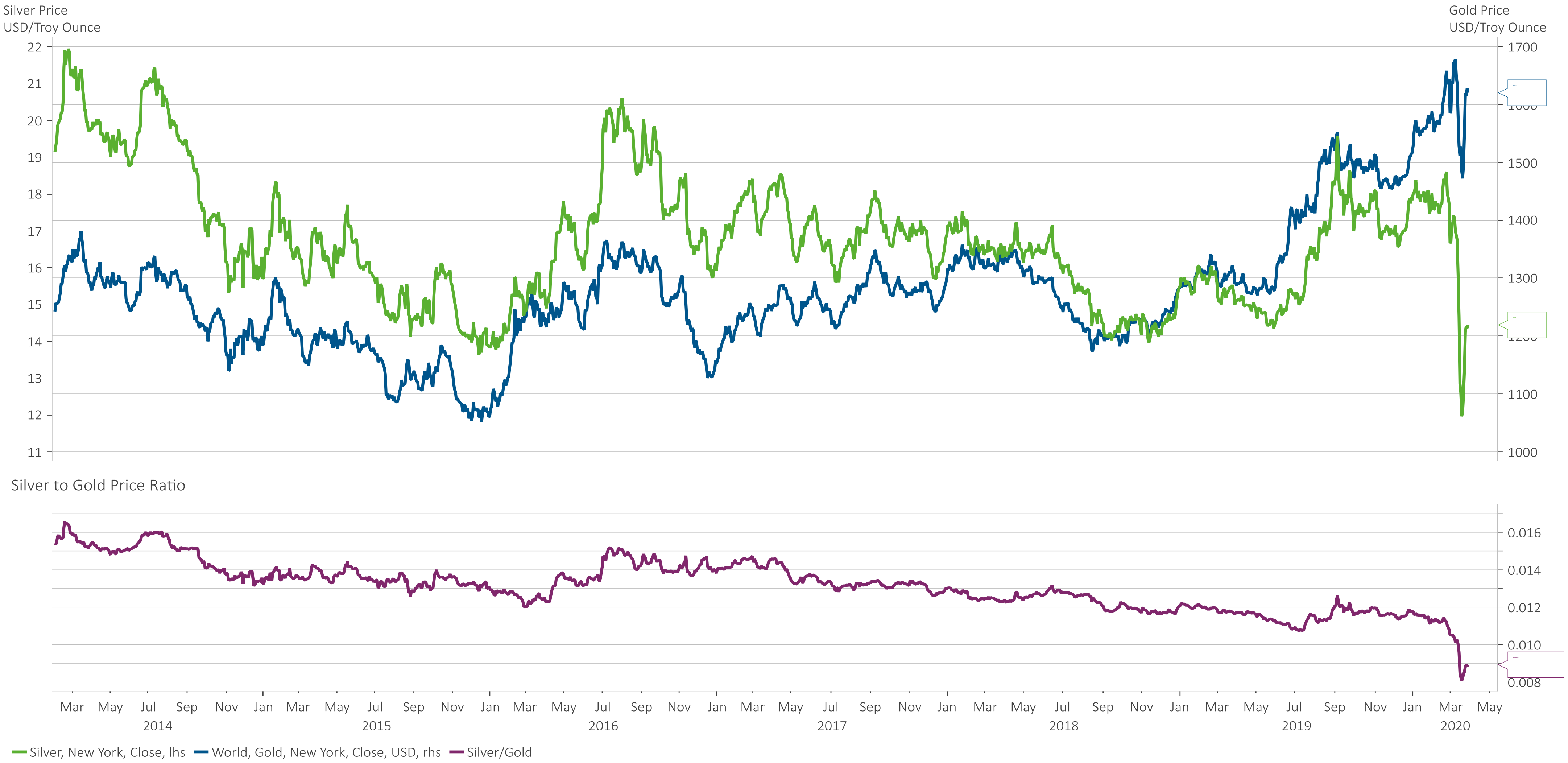
Source: Macrobond, S&P Dow Jones Indices, IHS Markit

Currency: USD Peaks Correspond With S&P 500 Bottoms; USD Remains Stronger Than '08 Highs.



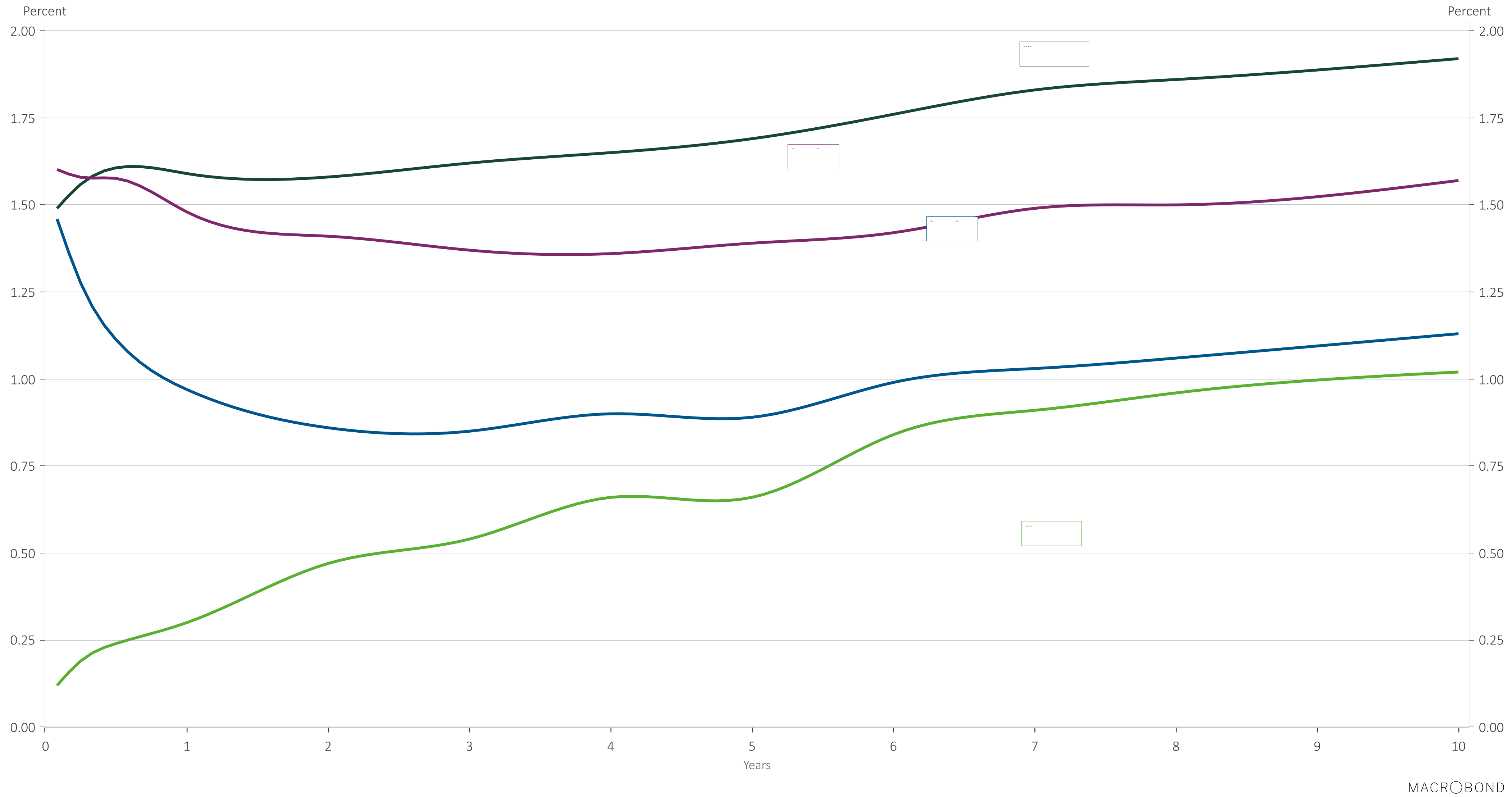
Source: Macrobond, S&P Dow Jones Indices, ICE

Commodities: Gold and Silver Rebound After Plummeting Despite Being Ultimate Insurance Plays



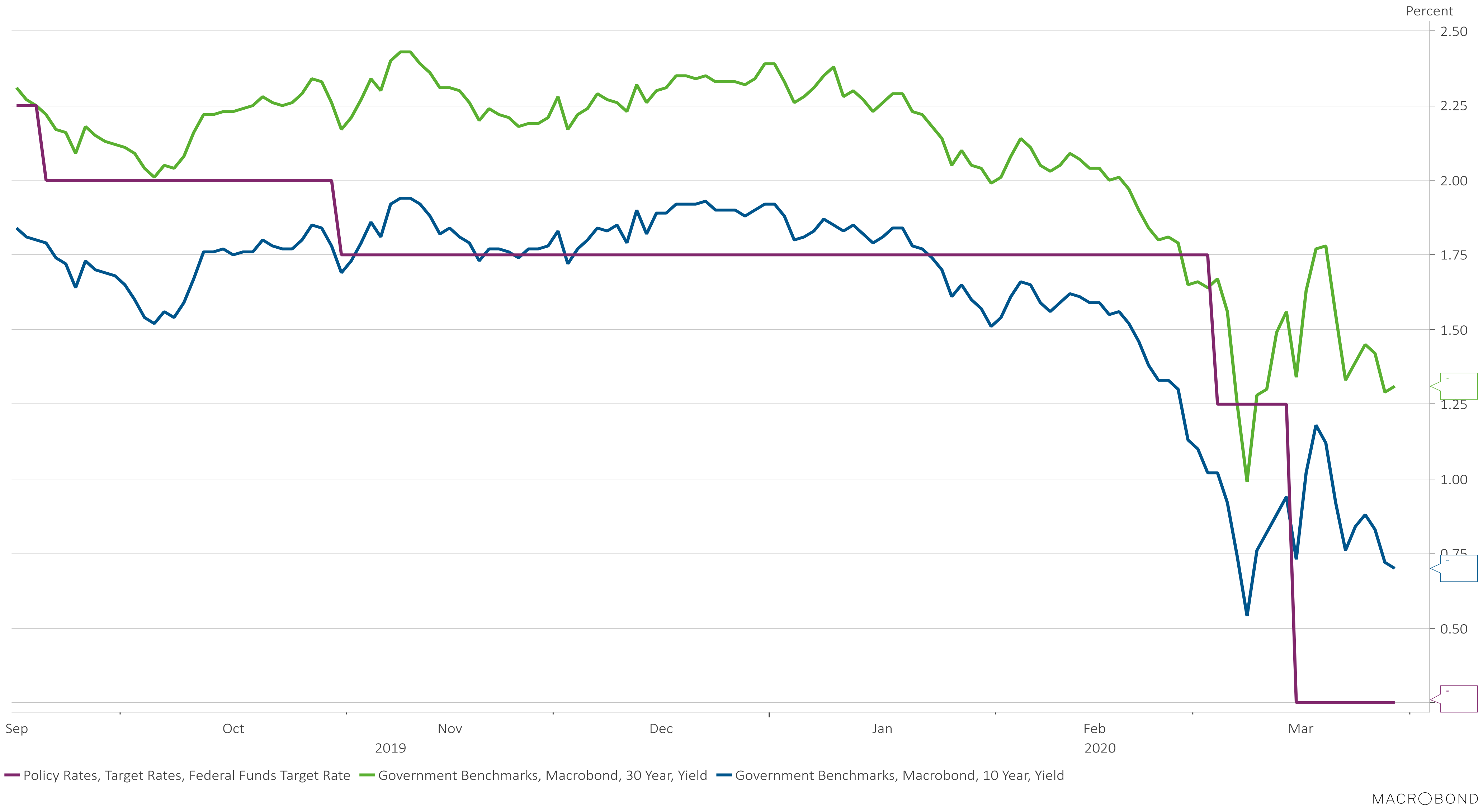
Source: Macrobond

Rates: Massive Monetary Stimulus Steepens U.S. Yield Curve



Source: Macrobond

Rates: U.S. Treasury Yields Volatile as Fed Slashes Policy Target Rate



Source: Macrobond, Federal Reserve

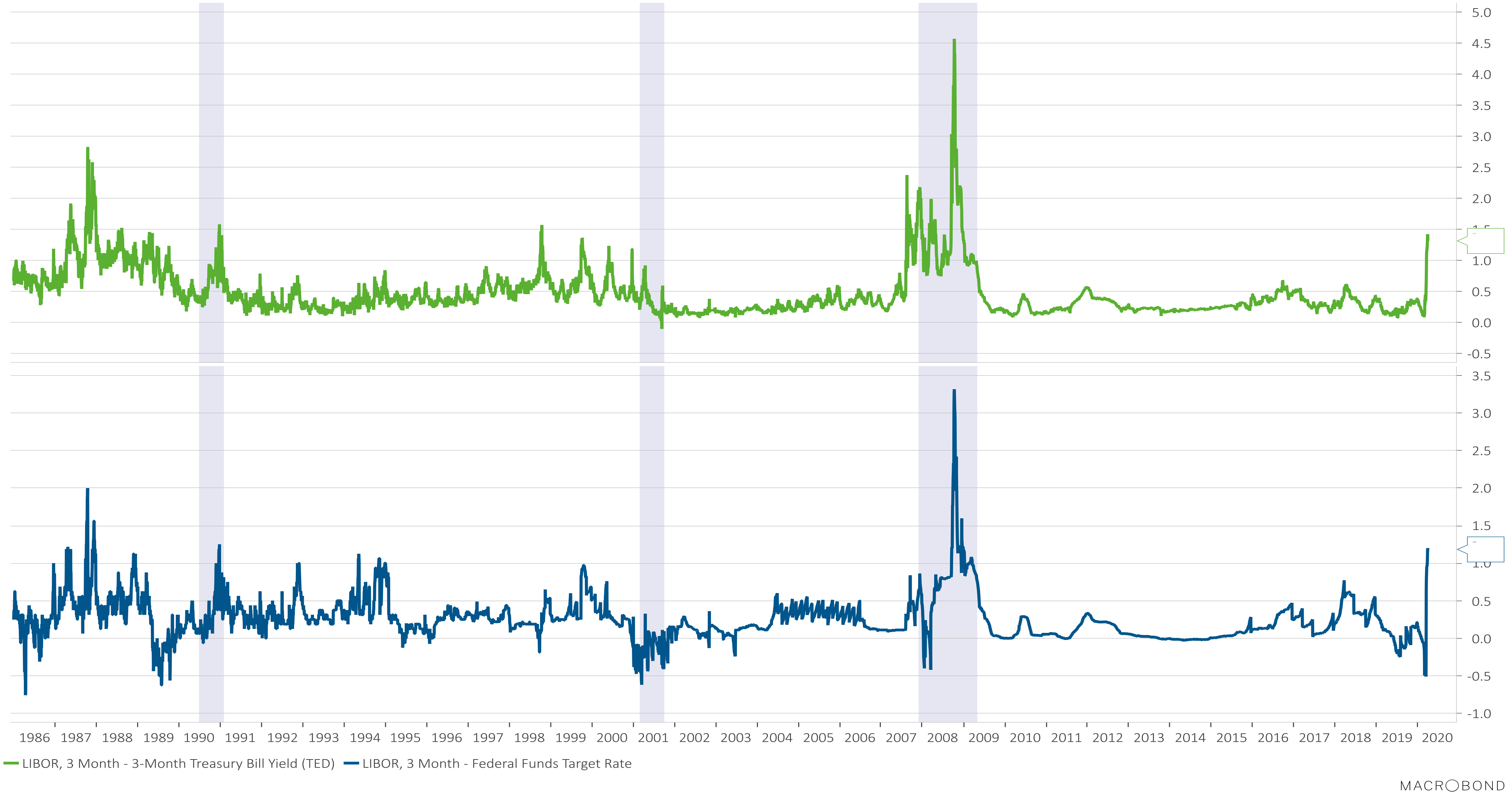
Rates: S&P 500 Dividend Yield Spreads Reach '08 Levels as Treasury Yields Fall, Making Dividend Paying Stocks Attractive

Source: Macrobond, S&P Dow Jones Indices

Rates: Inflation Expectations Rise Following Massive Economic Relief Packages

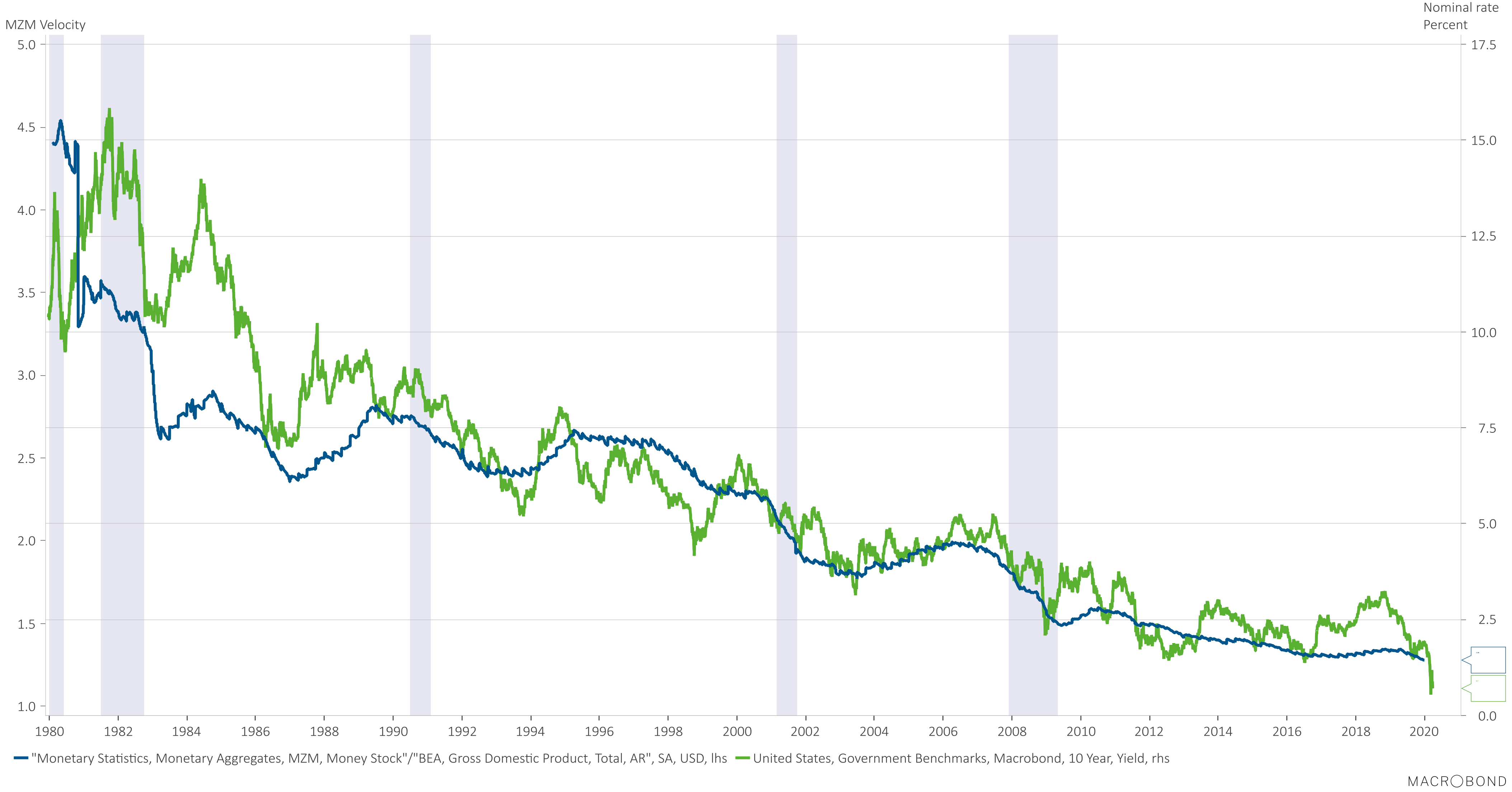
Source: Macrobond, Federal Reserve

Credit Risk: Overall Credit Risk (Ted Spread) & Banking Stress (LIBOR – Fed Funds Rate) Spike, But Remain Well Below '08 Levels of Stress



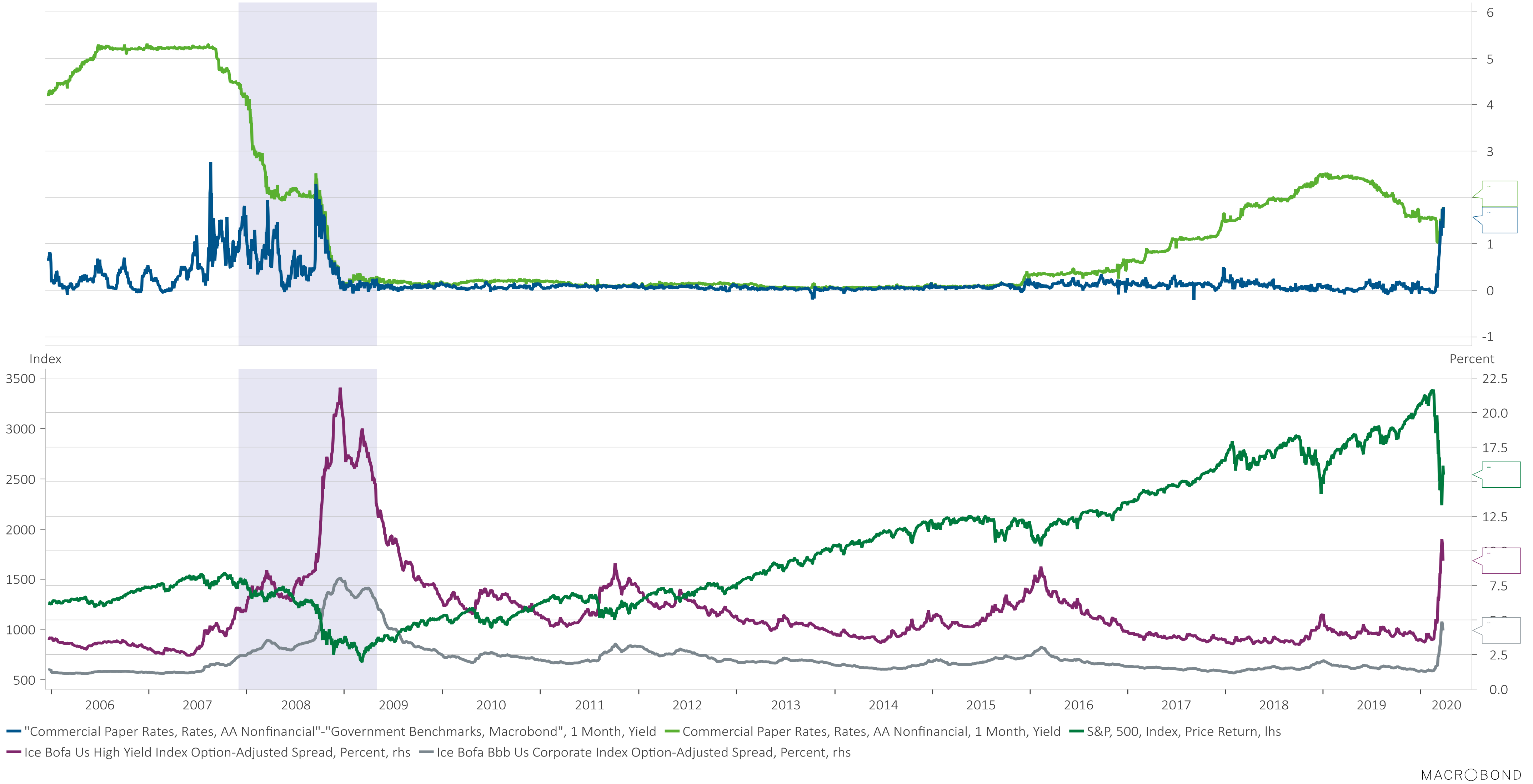
Source: Macrobond, Federal Reserve

Liquidity Risk: Money Velocity and Yields Fall to Historic Levels, Reducing Liquidity



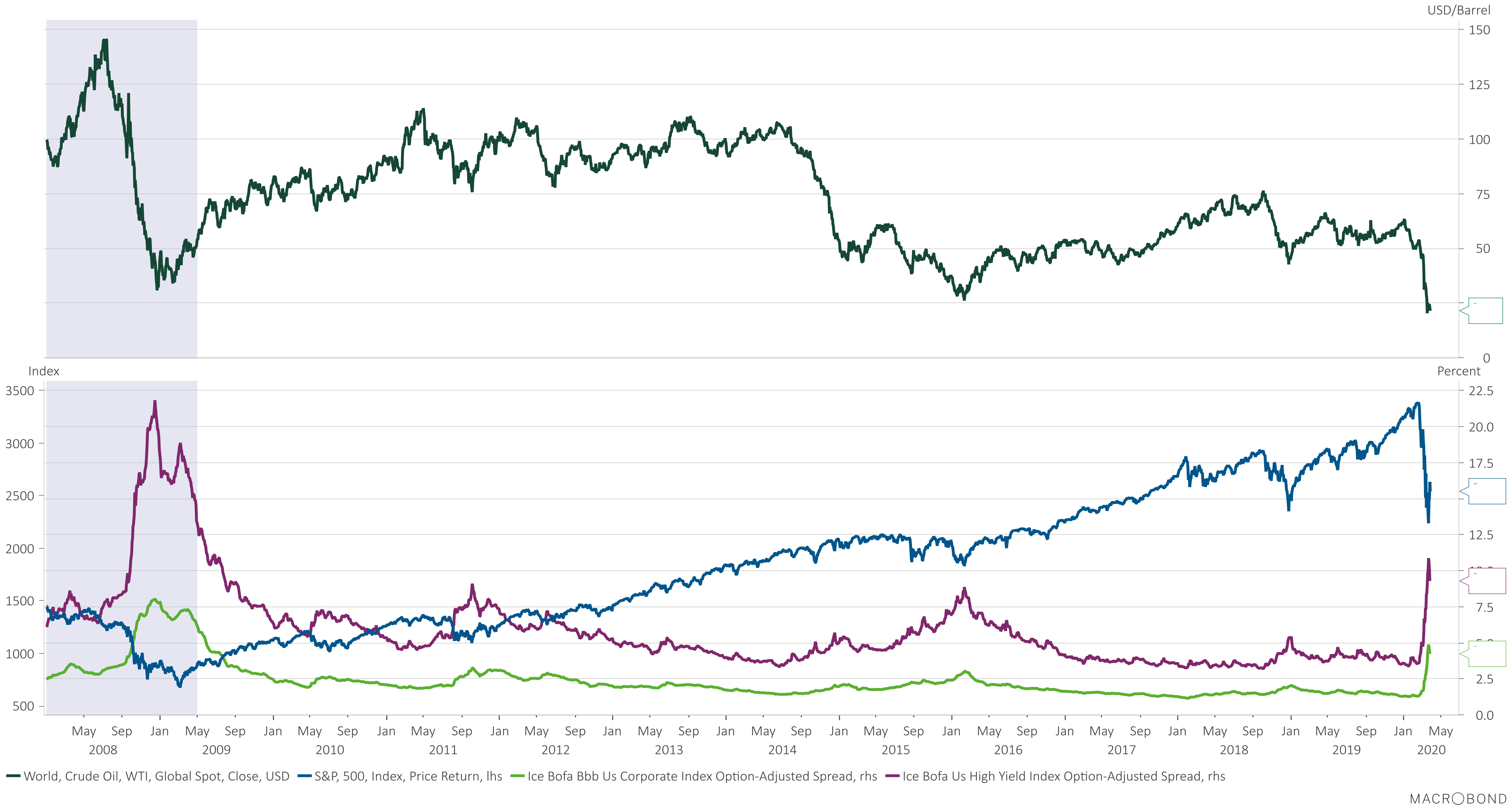
Source: Macrobond, Federal Reserve Bank of St. Louis, BEA

Liquidity Risk: The Fed Stabilizes Debt Markets as Commercial Paper Spreads Spike and HY Spreads Reached Distressed Levels



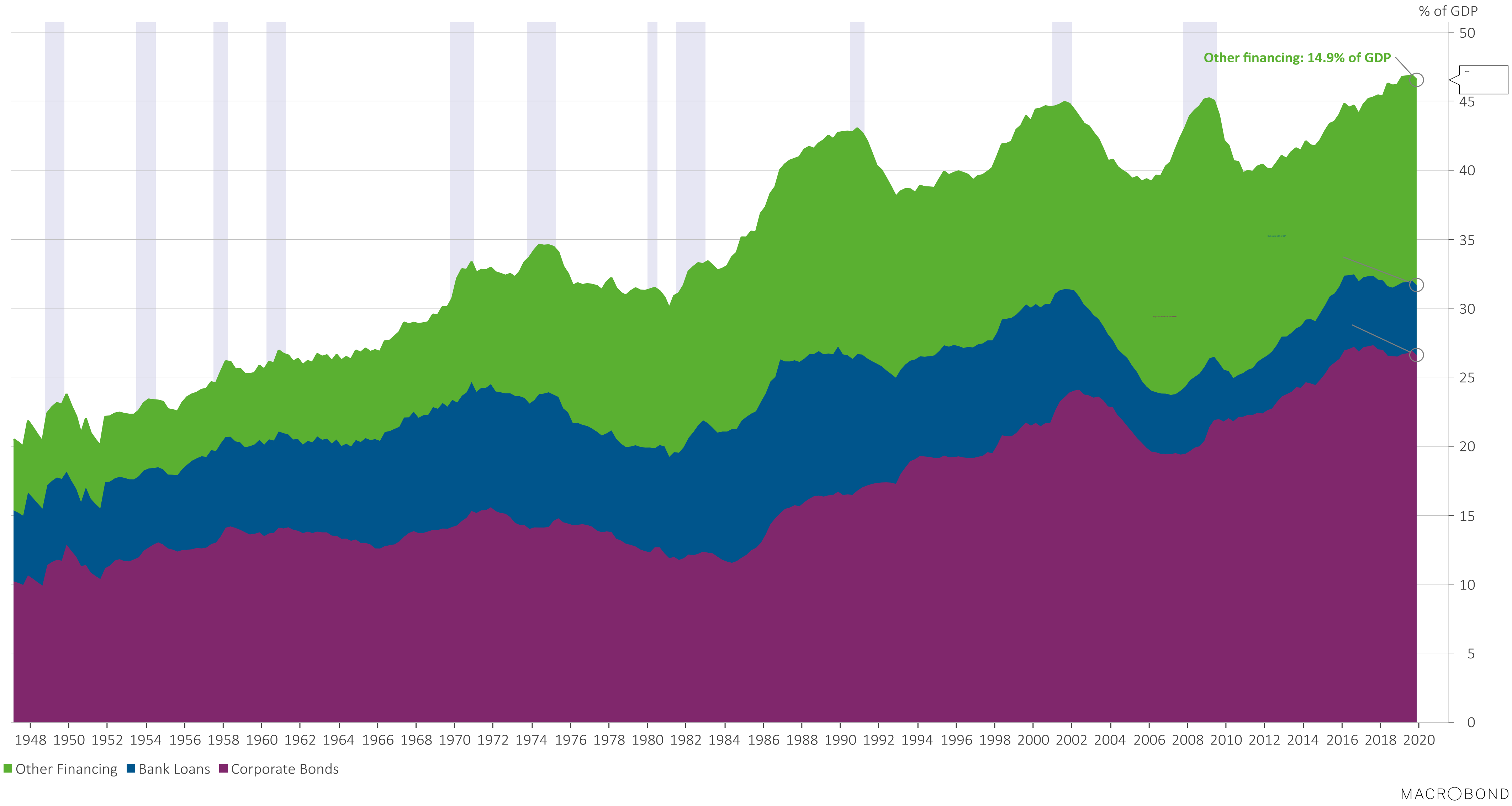
Source: Macrobond, Federal Reserve, S&P Dow Jones Indices, ALFRED

Credit Risk: HY Defaults Likely to Increase as Credit Spreads Spike to Distressed Levels and Oil Prices Plummet.



Source: Macrobond, S&P Dow Jones Indices, ALFRED

Credit Risk: Spiking Credit Spreads Are Likely to Expose Zombie Companies Who Survived During an Era of Low Rates.



Source: Macrobond, Federal Reserve, BEA

All Eyes On........

This week provided us with the first jaw-dropping release of economic data in the form of the historic jobless claims number and the Markit services flash PMI. Brace yourself for more of the same during the upcoming week as the coronavirus is sure to wreak havoc on the jobs report, jobless claims, PMIs, and ISM prints. Expectations or for historically bad prints on the upcoming data releases, however, it will be interesting how markets react considering equities rallied despite a historically bad jobless claims number this week.

Day	Event/Earnings
Monday, March 30	U.S. Pending Home Sales (February)
Tuesday, March 31	U.S. Case-Shiller Home Price Index (January), Chicago PMI (March), Consumer Confidence Index (March)
Wednesday, April 1	U.S. ADP Employment (March), Markit Manufacturing PMI (March), ISM Manufacturing Index (March)
Thursday, April 2	U.S. Weekly Jobless Claims (3/28), Factory Orders (February
Friday, April 3	U.S. Jobs Report (March), Markit Services PMI (March), ISM Nonmanufacturing Index (March)

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About Ryan Nauman

As Market Strategist, Ryan Nauman's primary focus is providing value added market and investment insight along with educating buy-side participants on investment analytics and portfolio management concepts.

Ryan provides analysis and research on market trends across asset classes, sectors, and regions to help empower better decisions for creating asset allocation strategies. His insight is disseminated through white papers, articles, training, and interviews with a target audience of financial advisors, portfolio managers, and investment analysts.

For more insights from Ryan:

Subscribe to his Weekly Recap here.